Raiffeisen RESEARCH

Central & Eastern European Strategy

1st quarter 2018

CEE on top of economic cycle

- Strongest growth since financial crisis continues 2018
- Keep an eye on imbalances in Turkey and Romania
- Interest rates environment tightening ahead of ECB
- Long CZK, buy 10y OFZ and POLGB on 3m horizon

Raiffeisen RESEARCH

www.raiffeisenresearch.com

Editor:

Peter Brezinschek, Raiffeisen Bank International AG, Vienna

peter.brezinschek@rbinternational.com

Raiffeisen RESEARCH

Central & Eastern European Strategy

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
BYN	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
PER	Price Earnings Ratio
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
OFZ	Russian 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
PX	Czech stock index
MOEX	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

Synchronised economic cycle, but divergent interest rate cycles

- **GDP estimates raised again for CE and SEE**
- **Russia on the way to modest growth**
- **Inflation targets to be achieved again in 2018, with some undershooting**

Thanks to renewed growth momentum since the middle of the year, we have once again upgraded some of our GDP estimates for the CE and SEE region. Poland and Romania in particular exhibit growth rates that are far higher than their respective potential rates. In both of these countries, it is mainly private consumption which is supporting this trend. Due to the loose fiscal policies, growth is also being driven by public consumption as well. Growth factors in the Czech Republic, Hungary, Slovakia, and Slovenia are much more balanced, as investment in plant and equipment is also a major component of economic growth in these countries. Nevertheless, it is clear that the robust growth in 2017 (CE average: 4.2%; SEE average: 5.0%) will be followed by strong growth in 2018 as well. The economic cycle in Austria shows a similar pattern: strong GDP growth of 3.2% in 2017 should also be followed by above-average growth of 2.6% in 2018. The positive momentum is being sustained by the unusually strong development of investment in plant and equipment. Including the boom starting from 2016, it appears that this will be the strongest phase for investments in the last 25 years. In Russia, GDP growth will likely remain stuck at below 2% in 2018.

Positive inflation rates will continue to make a comeback in the CEE region in 2018, driven by vigorous wage growth (partially related to increases in the minimum wage in Hungary and Romania) of between 4% and almost 10%, which cannot be underpinned by productivity gains in any of these countries. As a result, consumer prices will continue to rise, with increases between 2% and 3% anticipated in the CE region, although inflation figures will be distorted upwards in the SEE region, due to Romania (4.3%). In Russia, consumer price inflation should bottom out at a low of 2.5%. In the course of 2018, it is quite possible that the inflation rate will then rise towards the central bank's target of 4%.

Just as developments in inflation vary, there will also be significant differences in interest rate policies. The Czech central bank led the way as the first in the region and has already hiked its interest rates twice. The Romanian central bank is likely to follow starting from Q1 2018. We believe that Poland may also move ahead with initial rate hikes, but only in the second half of the year. By contrast, the Hungarian central bank will stick with its recently announced expansive measures until the ECB executes its turnaround. In Russia, there is still potential for rates to be lowered.

Impact on currencies: In principle, CZK and PLN should tend to be moderately stronger versus EUR over the course of the year, whereas HUF and RON may be more on the weak side. For the Russian rouble, we anticipate some mild depreciation versus USD and EUR, in line with additional rate cuts and a merely flat oil price trend.

Impact on the bond and equity markets: Analogously to EUR & USD bond yields, the extremely low yields in CE/SEE may rise slightly over a 12-month horizon. In Russia, the low point in yields will probably be reached during the course of 2018. The stock markets in CEE and Austria should also continue to be bolstered by the robust performance of the real economy and monetary factors. That said, one must keep an eye out for risks of higher price volatility as the year progresses. Taking a one-year view, we generally have Buy recommendations for the respective equity indices.

Financial analyst: Peter Brezinschek, RBI Vienna

CEE: Market strategy[1]

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

[1] **LCY bonds:** *based on absolute performance in LCY*
Eurobonds: *based on expected spread change*
FX *vs EUR*
Recommendation horizon: **end 1st quarter 2018**
For recommendation history please see page 56
B: Buy; H: Hold; S: Sell
2) HU: 3y, not 2y tenor
Source: RBI/Raiffeisen RESEARCH

Recommendations[1] – stock markets

Indices	
Buy	-
Hold	ATX, BIST Nat. 100, BUX, MOEX, PX, WIG 30
Sell	-

1 Recommendation horizon: end 1st quarter 2018
Source: RBI/Raiffeisen RESEARCH

Real GDP (% yoy)

Countries	2016	2017e	Consensus	2018f	Consensus	2019f	Consensus
Poland	2.7	4.4	4.2	4.1	3.8	3.6	3.4
Hungary	2.0	3.8	3.7	3.6	3.5	3.2	3.0
Czech Rep.	2.6	4.4	4.4	3.3	3.3	3.2	2.9
Slovakia	3.3	3.3	3.3	4.0	3.6	4.0	4.0
Slovenia	3.1	4.8	4.4	3.8	3.3	2.8	2.6
CE	**2.7**	**4.2**	4.1	**3.8**	3.6	**3.5**	3.3
Croatia	3.2	2.9	2.9	2.3	2.8	2.5	2.7
Bulgaria	3.9	4.0	3.6	4.2	3.5	4.0	3.0
Romania	4.8	6.8	5.7	4.2	3.9	3.5	3.5
Serbia	2.8	1.8	1.8	2.5	3.0	2.5	3.1
Bosnia a. H.	3.2	2.5	2.9	2.8	3.2	3.0	3.5
Albania	3.4	4.0	3.9	4.0	3.9	3.8	3.9
Kosovo	3.6	4.0	4.0	4.2	4.0	4.0	4.1
SEE	**4.1**	**5.0**	4.4	**3.7**	3.6	**3.3**	3.3
Russia	-0.2	1.8	1.8	1.5	1.8	1.5	1.7
Ukraine	2.3	1.9	2.0	2.5	3.0	3.0	2.9
Belarus	-2.6	2.0	1.5	1.5	1.7	2.0	1.9
EE	**-0.1**	**1.8**	1.8	**1.6**	1.9	**1.6**	1.8
Turkey	3.2	7.5	5.5	3.5	3.8	2.5	3.9
Austria	**1.5**	**3.2**	2.6	**2.6**	2.1	**1.6**	1.7
Germany	1.9	2.5	2.5	2.2	2.2	1.6	1.8
Euro area	**1.8**	**2.4**	2.3	**2.5**	2.1	**1.7**	1.8
USA	**1.5**	**2.4**	2.3	**2.5**	2.6	**2.0**	2.2

Source: national sources, RBI/Raiffeisen RESEARCH

Consumer prices (avg, % yoy)

Countries	2016	2017e	2018f	2019f
Poland	-0.6	2.0	2.3	2.6
Hungary	0.2	2.4	3.0	3.1
Czech Rep.	0.7	2.5	2.6	2.1
Slovakia	-0.5	1.3	2.1	2.0
Slovenia	-0.2	1.5	1.8	2.3
CE	**-0.2**	**2.1**	**2.4**	**2.5**
Croatia	-1.1	1.2	1.4	2.0
Bulgaria	-0.8	1.9	2.6	3.1
Romania	-1.5	1.3	4.3	3.3
Serbia	1.2	3.1	2.9	2.9
Bosnia a. H.	-1.1	1.3	1.8	2.0
Albania	1.3	2.0	2.4	3.0
Kosovo	0.3	1.6	1.5	1.7
SEE	**-0.9**	**1.6**	**3.3**	**2.9**
Russia	7.1	3.6	3.5	4.3
Ukraine	13.9	14.4	9.2	5.6
Belarus	12.0	8.0	7.5	8.0
EE	**7.7**	**4.5**	**4.0**	**4.5**
Turkey	7.8	11.0	9.5	8.0
Austria	**1.0**	**2.2**	**2.1**	**2.1**
Germany	0.4	1.7	2.2	1.9
Euro area	**0.2**	**1.5**	**1.3**	**1.7**
USA	**1.2**	**2.2**	**2.3**	**2.5**

Source: national sources, RBI/Raiffeisen RESEARCH

Current account balance (% of GDP)

Countries	2016	2017e	2018f	2019f
Poland	-0.3	-0.3	-1.0	-1.4
Hungary	5.4	3.2	2.9	2.7
Czech Rep.	1.1	1.1	0.7	0.4
Slovakia	-0.6	-0.6	0.1	1.2
Slovenia	5.2	6.5	6.3	5.5
CE	**0.7**	**0.4**	**0.0**	**-0.2**
Croatia	2.5	3.6	2.2	2.5
Bulgaria	3.7	6.9	5.5	4.4
Romania	-2.4	-3.3	-4.0	-4.3
Serbia	-3.9	-4.0	-4.2	-4.0
Bosnia a. H.	-4.4	-5.0	-5.9	-6.4
Albania	-9.1	-9.2	-9.4	-7.9
Kosovo	-8.3	-6.3	-7.5	-5.7
SEE	**-1.4**	**-1.3**	**-2.2**	**-2.4**
Russia	1.7	2.0	3.8	2.8
Ukraine	-4.1	-3.4	-4.2	-4.4
Belarus	-3.6	-3.5	-3.3	-3.2
EE	**1.2**	**1.5**	**3.0**	**2.2**
Turkey	-3.8	-4.7	-3.9	-4.2
Austria	**2.1**	**1.7**	**1.7**	**1.5**
Germany	8.2	7.5	7.5	7.0
Euro area	**3.3**	**3.1**	**2.8**	**2.7**
USA	**-2.4**	**-2.5**	**-2.5**	**-2.5**

Source: national sources, RBI/Raiffeisen RESEARCH

General budget balance (% of GDP)

Countries	2016	2017e	2018f	2019f
Poland	-2.4	-1.7	-1.8	-1.9
Hungary	-2.0	-2.5	-3.0	-3.0
Czech Rep.	0.6	0.0	-0.7	-0.4
Slovakia	-1.7	-1.5	-1.5	-1.5
Slovenia	-1.9	-0.9	-0.7	-0.5
CE	**-1.6**	**-1.4**	**-1.6**	**-1.6**
Croatia	-0.9	-0.5	-1.0	-1.3
Bulgaria	1.6	-0.5	-1.0	-1.5
Romania	-3.0	-3.0	-3.5	-3.0
Serbia	-1.3	-0.5	-0.8	-1.0
Bosnia a. H.	1.2	1.0	-0.5	0.5
Albania	-2.5	-2.0	-2.0	-1.0
Kosovo	-1.6	-2.0	-2.0	-1.5
SEE	**-1.6**	**-1.8**	**-2.3**	**-2.1**
Russia	-3.7	-2.5	-2.0	-1.5
Ukraine	-2.9	-3.1	-2.6	-2.2
Belarus	1.5	1.0	1.0	0.5
EE	**-3.5**	**-2.4**	**-1.9**	**-1.5**
Turkey	-1.4	-2.5	-2.0	-2.0
Austria	**-1.6**	**-0.7**	**-0.7**	**-0.6**
Germany	0.8	0.5	0.3	0.5
Euro area	**-1.5**	**-1.1**	**-0.9**	**-0.8**
USA	**-3.2**	**-3.5**	**-2.6**	**-3.0**

Source: national sources, RBI/Raiffeisen RESEARCH

Public debt (% of GDP)

Countries	2016	2017e	2018f	2019f
Poland	54.3	52.6	51.3	50.5
Hungary	73.9	72.9	71.9	71.1
Czech Rep.	37.9	34.3	33.1	31.8
Slovakia	51.9	52.0	50.9	49.5
Slovenia	78.5	76.2	74.7	73.9
CE	**54.4**	**52.5**	**51.3**	**50.4**
Croatia	82.7	79.8	77.4	74.9
Bulgaria	29.1	25.0	25.0	26.0
Romania	37.6	36.7	37.2	37.9
Serbia	71.6	62.8	60.5	57.5
Bosnia a. H.	40.4	40.8	40.0	41.5
Albania	71.0	71.0	69.0	65.0
Kosovo	14.5	17.5	19.0	19.0
SEE	**47.1**	**44.7**	**44.3**	**44.1**
Russia	13.5	13.0	13.0	13.2
Ukraine	76.1	70.1	62.9	59.5
Belarus	39.0	39.0	40.5	40.5
EE	**18.4**	**17.6**	**17.0**	**17.1**
Turkey	32.0	33.0	32.0	32.0
Austria	**83.6**	**77.9**	**75.1**	**72.8**
Germany	68.1	65.8	63.3	61.3
Euro area	**88.9**	**87.2**	**85.2**	**83.3**
USA	**105.5**	**105.6**	**104.9**	**104.7**

Source: national sources, RBI/Raiffeisen RESEARCH

Gross foreign debt (% of GDP)

Countries	2016	2017e	2018f	2019f
Poland	74.5	72.7	71.1	65.6
Hungary	98.3	88.2	83.1	77.3
Czech Rep.	73.9	89.6	86.6	83.5
Slovakia	88.8	96.2	93.8	91.5
Slovenia	110.9	99.2	95.1	90.3
CE	**66.7**	**68.1**	**66.2**	**62.0**
Croatia	89.8	82.5	79.7	76.3
Bulgaria	72.1	63.7	61.3	60.4
Romania	54.8	50.8	50.4	51.2
Serbia	74.2	66.7	63.9	62.5
Bosnia a. H.	54.3	54.8	54.2	53.1
Albania	71.7	67.4	64.7	59.8
Kosovo	34.8	34.7	34.5	35.5
SEE	**64.4**	**59.1**	**57.7**	**57.1**
Russia	39.0	29.3	25.8	22.6
Ukraine	121.7	102.4	93.3	88.5
Belarus	79.3	73.4	73.7	73.0
EE	**45.8**	**35.2**	**31.8**	**28.6**
Turkey	47.5	47.7	46.7	45.3
Austria	**n.v.**	**n.v.**	**n.v.**	**n.v.**
Germany	n.v.	n.v.	n.v.	n.v.
Euro area	**127.7**	**124.5**	**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	2016	2017e	2018f	2019f
Poland	4.36	4.26	4.16	4.20
Hungary	311	309	317	320
Czech Rep.	27.0	26.4	25.2	24.9
Slovakia	euro	euro	euro	euro
Slovenia	euro	euro	euro	euro
Croatia	7.53	7.46	7.46	7.48
Bulgaria	1.96	1.96	1.96	1.96
Romania	4.49	4.57	4.67	4.68
Serbia	123	121	121	123
Bosnia a. H.	1.96	1.96	1.96	1.96
Albania	137	134	135	136
Kosovo	euro	euro	euro	euro
Russia	74.1	66.4	73.6	81.8
Ukraine	28.3	30.3	33.3	37.0
Belarus	2.20	2.20	2.51	2.88
Turkey	3.34	4.13	4.68	5.29
Austria	**euro**	**euro**	**euro**	**euro**
Germany	euro	euro	euro	euro
Euro area	**euro**	**euro**	**euro**	**euro**
USA	**1.11**	**1.14**	**1.20**	**1.28**

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Ratings[1]

Countries	S&P	Moody's	Fitch
Poland	BBB+	A2	A-
Hungary	BBB-	Baa3	BBB-
Czech Rep.	AA-	A1	A+
Slovakia	A+	A2	A+
Slovenia	A+	Baa1	A-
Croatia	BB	Ba2	BB
Bulgaria	BBB-	Baa2	BBB
Romania	BBB-	Baa3	BBB-
Serbia	BB-	Ba3	BB-
Bosnia a. H.	B	B3	NR
Albania	B+	B1	NR
Kosovo	NR	NR	NR
Russia	BB+	Ba1	BBB-
Ukraine	B-	Caa2	B-
Belarus	B	Caa1	B-
Turkey	BB	Ba1	BB+
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	14-Dec[1]	Mar-18	Jun-18	Dec-18
vs EUR				
Poland	4.22	4.15	4.10	4.20
Hungary	313.71	315.0	315.0	320.0
Czech R.	25.71	25.2	24.8	25.0
Croatia	7.55	7.45	7.40	7.50
Romania	4.63	4.65	4.65	4.70
Serbia	119.24	121.0	121.0	122.0
Albania	133.38	134.0	135.0	135.0
vs USD				
Russia	58.8	59.0	60.0	64.0
Ukraine	27.44	28.00	27.50	28.50
Belarus	2.03	2.03	2.07	2.21
Turkey	3.88	3.80	3.90	4.00
EUR/USD	1.18	1.15	1.20	1.24

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

Key interest rate forecast

Countries	14-Dec[1]	Mar-18	Jun-18	Dec-18
Poland	1.50	1.50	1.50	2.00
Hungary	0.90	0.90	0.90	0.90
Czech R.	0.50	0.75	1.00	1.25
Romania	1.75	2.25	2.50	3.00
Russia	7.75	7.50	7.00	6.75
Turkey	8.00	8.00	8.00	8.00
Euro area	0.00	0.00	0.00	0.00
USA	1.50	1.50	1.75	2.25

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

3m money market rate forecast

Countries	14-Dec[1]	Mar-18	Jun-18	Dec-18
Poland	1.72	1.73	1.90	2.40
Hungary	0.03	0.05	0.05	0.20
Czech R.	0.76	1.10	1.25	1.60
Croatia	0.56	0.55	0.55	0.60
Romania	2.13	2.50	2.75	3.30
Russia	8.33	7.62	7.40	7.15
Turkey	14.60	13.00	13.20	14.00
Euro area	-0.33	-0.35	-0.35	-0.10
USA	1.60	1.60	1.85	2.35

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

2y LCY yield forecast

Countries	14-Dec[1]	Mar-18	Jun-18	Dec-18
Poland	1.66	2.1	2.2	2.4
Hungary*	0.67	0.6	0.7	1.0
Czech R.	0.23	0.5	0.8	1.2
Croatia	0.60	0.5	0.6	0.7
Romania*	3.45	3.8	4.0	4.2
Russia	7.20	7.3	7.1	7.0
Turkey	13.16	12.3	12.5	13.5
Austria	-0.60	-0.6	-0.6	-0.3
Germany	-0.76	-0.7	-0.7	-0.4
USA	1.81	1.9	2.1	2.4

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

10y LCY yield forecast

Countries	14-Dec[1]	Mar-18	Jun-18	Dec-18
Poland	3.23	3.4	3.4	3.6
Hungary	2.23	2.2	2.3	2.4
Czech R.	1.43	1.9	2.0	2.2
Croatia	2.34	2.5	2.5	2.5
Romania	4.43	4.6	4.8	5.0
Russia	7.62	7.6	7.5	7.3
Turkey	11.98	11.0	11.0	12.0
Austria	0.49	0.7	1.0	1.2
Germany	0.32	0.5	0.8	1.0
USA	2.35	2.5	2.8	3.0

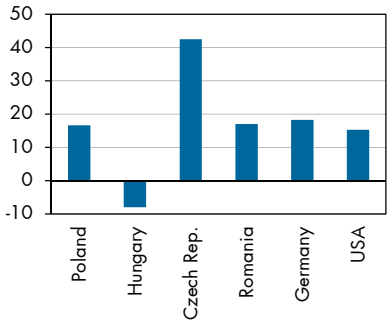
[1] 5:00 p.m. (CET)
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Spreads 10y LCY bonds over Bund

Countries	14-Dec[1]	Mar-18	Jun-18	Dec-18
Poland	292	290	260	260
Hungary	191	165	145	140
Czech R.	111	135	120	120
Croatia	202	200	170	150
Romania	411	410	400	400
Russia	730	700	670	630
Turkey	1166	1050	1020	1100
Austria	17	20	20	20
USA	203	200	200	200

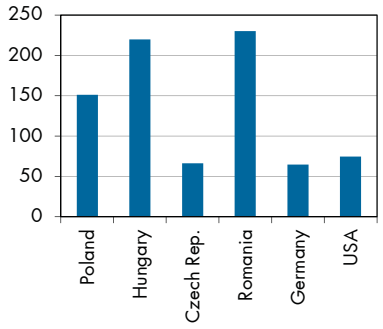
[1] 5:00 p.m. (CET); all values in bp
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Expected 10y LCY yield change



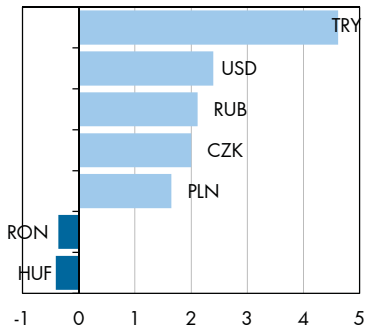
bp-change of 10y gov. bond yield in next 3 months
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Yield structure



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

LCY changes vs EUR (% qoq)[1]



[1] forecasts for 31 Mar-2017 in comparison to 15 Dec-2016
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Stock market indicators

	Earnings growth		Price/earnings ratio	
	17e	18f	17e	18f
ATX	31.9%	11.2%	14.0	12.6
WIG 30	21.2%	3.7%	12.4	12.0
BUX	6.1%	3.2%	10.7	10.4
PX	19.7%	-12.7%	12.2	13.9
MOEX	8.8%	10.0%	7.4	6.8
BIST Nat. 100	48.5%	10.2%	8.9	8.0

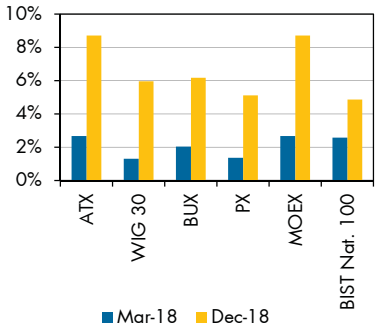
Source: Thomson Reuters, IBES, Bloomberg, RBI/Raiffeisen RESEARCH

Stock market forecasts

	Index estimates			
	14-Dec[1]	Mar-18	Jun-18	Dec-18
ATX	3,311	3,400	3,520	3,600
WIG 30	2,794	2,830	2,980	2,960
BUX	38,616	39,400	41,200	41,000
PX	1,065	1,080	1,120	1,120
MOEX	2,152	2,210	2,290	2,340
BIST Nat. 100	109,666	112,500	115,500	115,000

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

Expected index performance

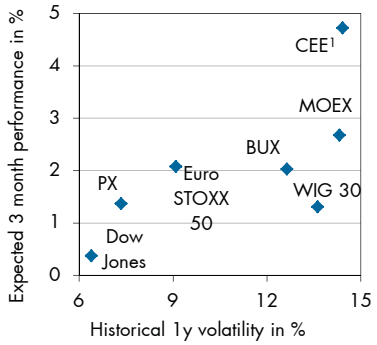


Source: RBI/Raiffeisen RESEARCH

CEE remains an attractive region for investment

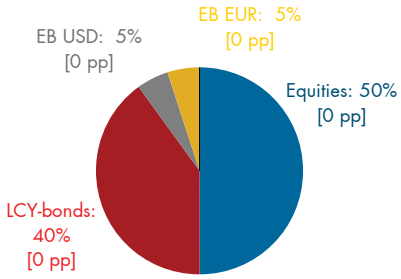
- **Buy recommendation for CEE equity markets in 2018, overweight vs developed markets**
- **CEE bonds also show better potential for returns**
- **Short-term assessment of the equity market is neutral, in light of correction risks**

Risk-return (%)



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

CEE portfolio weightings Q1 2018



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

All in all, the **stock markets in Eastern Europe can look back on positive performance in the fourth quarter**, and the annual performance of these markets was quite impressive in 2017. Looking to **2018, conditions still look promising** for the equity markets in Eastern Europe, thanks to strong local economic growth, (still) no inflationary pressure and thus (still) only moderate measures by the central banks in the region, equity market valuations which range from moderate (CE) to cheap (RU, TR), and in particular the generally supportive conditions anticipated for global equity markets in the first half of the year. Over the short term, however, we believe that a great deal of optimism has already been priced in on the global markets, and consequently we **generally take a neutral stance on the equity markets for the start of the year**, waiting for better buying opportunities to arise in Q1. These opportunities may emerge on the two cheapest equity markets in the region in particular: in Russia due to a correction in oil prices and in Turkey as a result of renewed turbulence for the currency. **Over a one-year horizon, all of these markets deserve a "Buy"** in our opinion. Looking at **bonds**, however, the situation is much more **complicated**: While currencies such as **PLN and CZK** have more **potential for appreciation** over a one-year horizon (thanks in part to more hikes in interest rates), **depreciation risks** tend to have the upper hand **in Hungary**. The **rouble appears** to be very **attractive**, due to the high interest rates, but **by the middle of the year** profit-taking will make sense, before the USD, which should appreciate versus euro in the second half of the year, also strengthens versus the rouble (for now, still clearly a Buy). **Turkey** features the highest interest rates in the region and the highest level of political risk and thus this market remains a question of faith: the high interest rate level justifies an overweight position over the short term (Q1), which – however – we would quickly close again after any brief appreciation of the exchange rate. With negative performance expectations for EUR government bonds in 2018, the **CEE region** thus remains an important component in portfolios in the **bond segment** and deserves to be **overweighted**.

Financial analyst: Valentin Hofsätter, CFA, RBI Vienna

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	7.7	7.3	11.6	6.1	-4.4	-4.0	0.0	3.0	1.2	-3.8	4.5	4.6
Hungary	15.3	14.8	16.2	18.1	10.2	12.4	3.7	1.5	4.0	5.6	5.8	8.0
Poland	13.9	13.0	30.2	24.5	-0.7	-0.1	4.0	1.7	9.7	4.9	-8.6	-8.0
Romania[4]	10.8	10.6	5.2	7.2	12.4	13.2	2.5	0.6	-1.6	0.3	-2.0	0.4
Russia	17.1	14.8	-10.4	-3.0	-3.3	5.0	9.7	1.8	4.6	12.4	-3.0	8.1
Turkey	28.3	20.6	12.4	37.7	-6.6	6.8	17.6	6.8	-15.0	4.2	-8.3	4.8
Croatia	11.6	11.6	-1.3	-1.5	0.3	0.4	1.6	1.9	9.1	8.9	6.7	6.8
CEE	11.0	-	7.1	-			2.8	-	4.6	-		

[1] MSCI indices; [2] Three months volatility annualised; [3] Five-year annual return
[4] Performance 5y: in case of Romanian bonds, data available only since 13 July 2015
LCY…local currency
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Prospects for CEE local debt markets dominated by FX outlook

- **We put Russia on overweight with RUB risks increasing in H2 though**
- **Other high-yielder Turkey as a speculative Buy as disinflation to brighten s/t prospects for TURKGBs**
- **In CEE low-yielders POLGBs most attractive in our view mainly due to expected PLN gains**

Given our call for a slightly stronger USD versus the EUR in the short-term, EUR-based **OFZ market investors in particular could post moderate gains** on our investment horizon to the end of Q1 2018. The longer-term outlook is clouded though since significant rouble weakening is expected that could easily erase the expected price gains in the course of 2018. While rate cuts could continue at a faster and deeper pace than earlier anticipated, much of this is already priced into RUB bonds.

As a **speculative overweight in the high-yielding universe we recommend TURKGB**. We reckon that the Turkish central bank, which disappointed markets by delivering less tightening than hoped for in December, is banking on the expected start of a significant disinflation process. This should turn real yields positive in the course of Q1 2018. As we think this strategy has a good chance of working, we are speculating on another bout of TRY relief in the course of Q1, also triggering TURKGB gains.

In the CE/SEE low-yielding markets we are neutral across the board with the exception of a **tactical overweight for CZGBs**. Adding exposure on EUR/CZK dips and / or spikes in yield spreads vs DE should be an appropriate strategy to use CZGBs as a physical vehicle to play CZK appreciation bets.

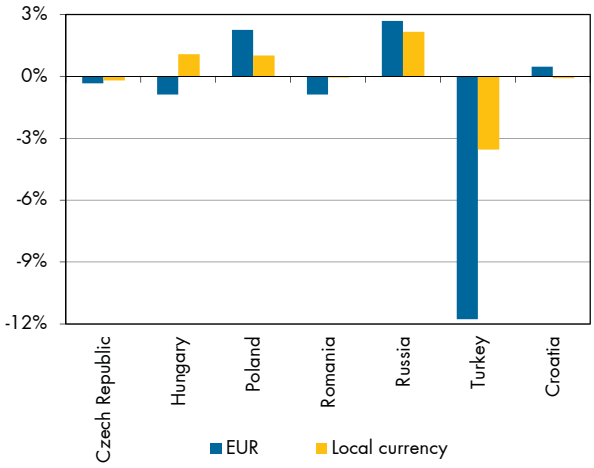
Financial analyst: Stepahn Imre; RBI Vienna

Portfolio weightings: bonds*

	Portfolio	Benchmark	Difference
EB USD	10.0%	10.0%	0.0%
EB EUR	10.0%	10.0%	0.0%
LCY	80.0%	80.0%	0.0%
Czech Republic	20.0%	20.0%	0.0%
Hungary	19.0%	20.0%	-1.0%
Poland	46.0%	45.0%	1.0%
Romania	1.0%	5.0%	-4.0%
Russia	8.0%	5.0%	3.0%
Turkey	6.0%	5.0%	1.0%
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

Expected bond market performance (%)

	3m		6m		9m		12m	
Countries	**EUR**	**LCY**	**EUR**	**LCY**	**EUR**	**LCY**	**EUR**	**LCY**
Czech Republic	0.9	-1.0	1.6	-1.8	-1.7	-3.1	0.1	-2.5
Hungary	0.5	0.8	0.4	0.7	-1.4	0.5	-1.1	0.8
Poland	1.0	-0.6	2.9	0.1	1.5	-0.1	0.2	-0.2
Romania	-0.2	0.2	-0.4	0.0	-0.9	0.6	-0.3	1.2
Russia	5.4	2.9	1.2	4.9	-7.7	7.5	-5.6	10.0
Turkey	22.0	8.8	18.0	11.6	14.8	11.7	11.6	11.7

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

Turkey is our speculative overweight position in Q1

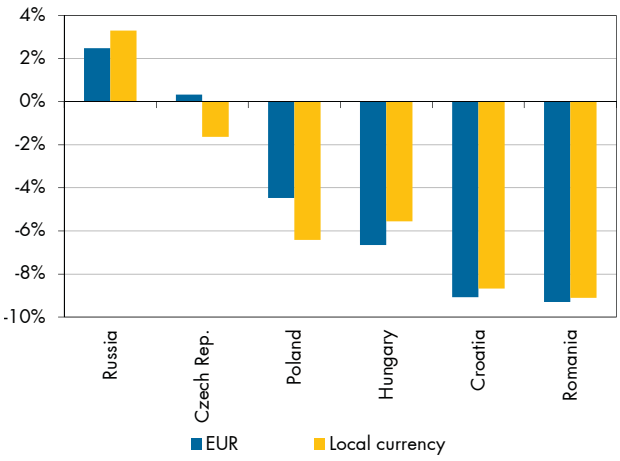
- **Fundamentals look strong for the BIST 100, but political risks are not off the table**
- **However, given our call for an appreciating TRY over the short-term, we recommend a speculative overweight for Turkish equities**
- **Wage pressure could weigh on Polish corporate earnings**

Portfolio weightings: stocks*

	Portfolio	Benchmark	Difference
Czech Rep.	8.0%	8.0%	0.0%
Hungary	7.0%	7.0%	0.0%
Poland	23.0%	25.0%	-2.0%
Russia	35.0%	35.0%	0.0%
Turkey	27.0%	25.0%	2.0%
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

The **BIST 100** index is still the strongest market in our equity market universe, having posted a gain of 40% in LCY since the beginning of the year. The economic data had already been pointing to acceleration and the very strong GDP growth figures delivered for Q3 have confirmed this development. Although the economic performance looks impressive, one must also keep in mind that it has been accompanied by very high inflation recently (November 2017: 13% yoy) and a steadily weakening currency. Moreover, politics is a factor of uncertainty that must be reckoned with (disputes with the EU and the USA). The expected aggregate earnings growth is estimated at 10.2% for 2018f, and in light of the economic growth this figure is quite plausible. The 2018f PER calculated on this basis amounts to 8.0, and this looks relatively cheap to use, despite the risk discount which must be taken into consideration. Given our call for a rebound in the TRY in Q1 and the attractive fundamentals we recommend a speculative overweight in Turkish stocks over the short-term, despite the fact that political risks are not off the table.

Even though the **Polish stock market** was among the best compared to the CE-3 countries in 2017, we expect a somewhat lower, albeit positive performance for the next quarter. Whereas the economic environment remains benign, locally as well as globally seen, wage pressure could weigh on corporate earnings. Whereas for 2017 the estimated earnings growth should be around 21%, 2018 earnings should rise only by 3.7%. Moreover, the political disputes with the EU should continue, but the negative impact on the market should be limited. Consequently, we underweight the Polish stock market, due to the lower performance forecast compared to peers.

Financial analyst: Andreas Schiller, CFA, RBI Vienna

Expected stock market performance (%)

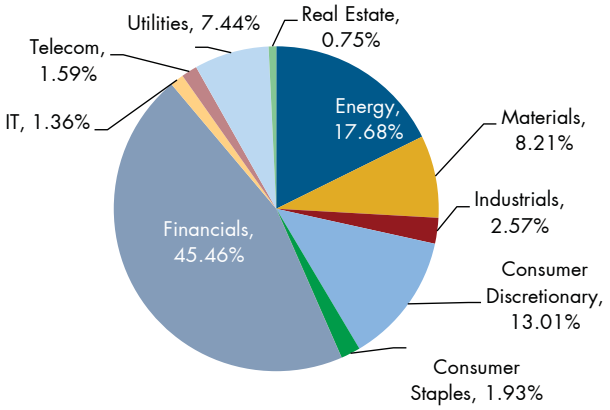
	3m		6m		9m		12m	
Countries	**EUR**	**LCY**	**EUR**	**LCY**	**EUR**	**LCY**	**EUR**	**LCY**
Czech Republic	3.3	1.4	8.9	5.1	-0.9	-2.4	8.0	5.1
Hungary	1.7	2.0	6.4	6.7	-3.4	-1.6	4.2	6.2
Poland	3.0	1.3	9.8	6.7	-0.7	-2.3	6.4	6.0
Russia	5.2	2.7	2.7	6.4	-12.9	-0.6	-4.8	8.7
Turkey	16.8	2.6	11.7	5.3	6.5	3.5	4.7	4.9

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

Sector weightings in comparison

Sector weightings Poland, WIG 30

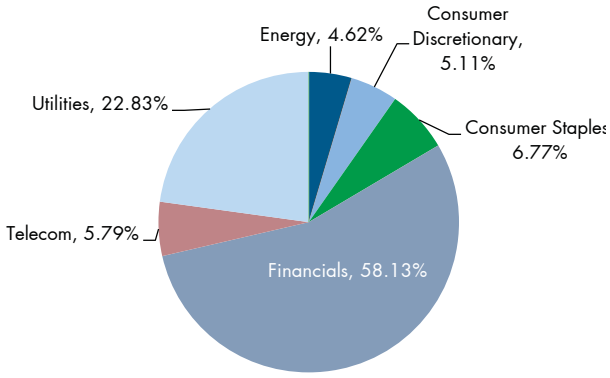
Dom. market cap.: EUR 162.25 bn (Source: Bloomberg; 14/12/2017)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Sector weightings Czech Republic, PX

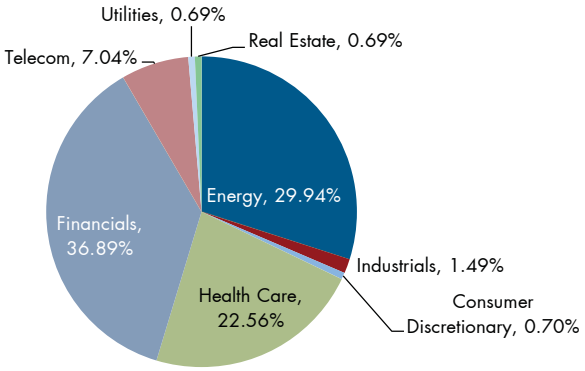
Dom. market cap.: : EUR 27.76 bn (Source: Bloomberg; 14/12/2017)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Sector weightings Hungary, BUX

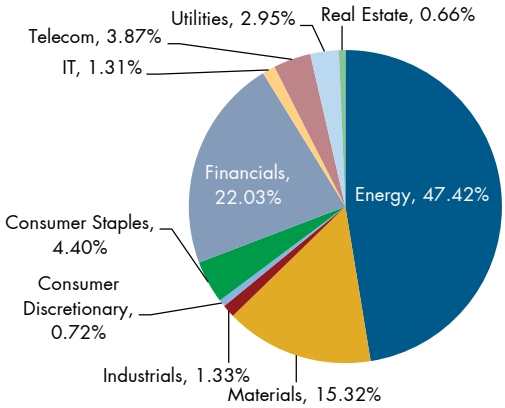
Dom. market cap.: : EUR 25.25 bn (Source: Bloomberg; 14/12/2017)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Sector weightings Russia, MOEX

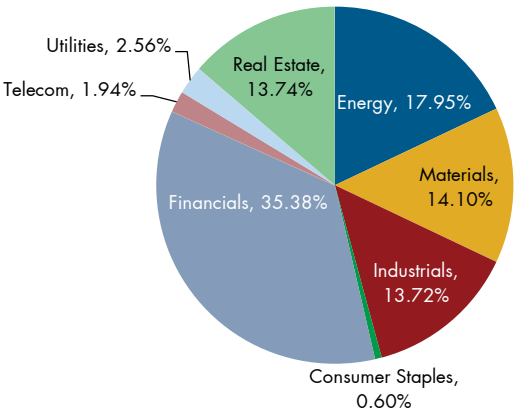
Dom. market cap.: EUR 494.72 bn (Source: Bloomberg; 14/12/2017)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Sector weightings Austria, ATX

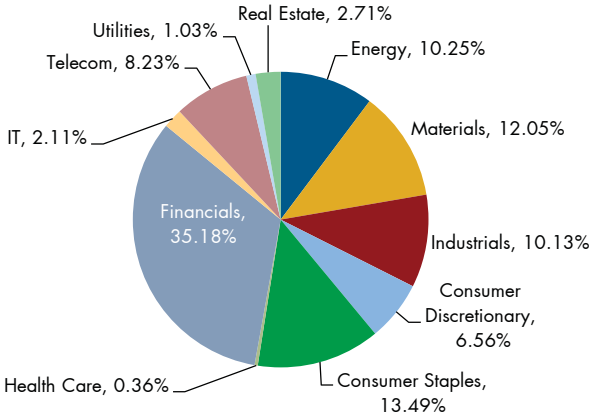
Dom. market cap.: EUR 125.14 bn (Source: Bloomberg; 14/12/2017)



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Sector weightings Turkey, BIST National 100

Dom. market cap.: EUR 175.53 bn (Source: Bloomberg; 14/12/2017)

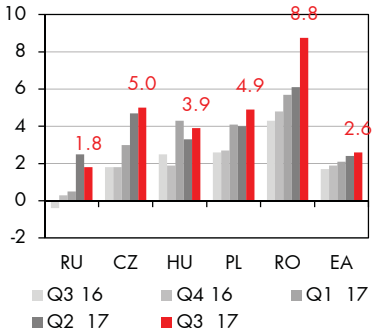


Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Another round of upwards growth revisions

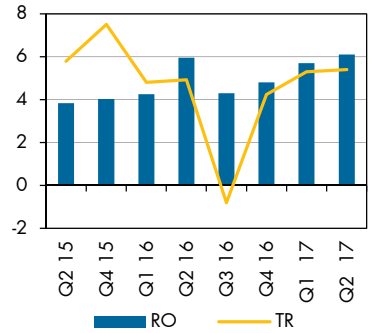
- **Strong, broad-based economic upswing in CE/SEE to continue in 2018/2019**
- **High wage growth not expected to drive prices up, we uphold moderate inflation projections**
- **CE/SEE nudged into tightening mode; differentiation with CZ and RO first, followed by PL; HU delayed**
- **Fiscal policy still exhibiting pro-cyclical bias, focus on Romania and Hungary**

CEE GDP growth (% yoy)



Source: Bloomberg, RBI/Raiffeisen RESEARCH

Turkey, Romania overheating*



** GDP, % yoy*
Source: Bloomberg, RBI/Raiffeisen RESEARCH

CEE quarterly growth rates (% yoy)

	Q1 17	Q2 17	Q3 17
CZ	3.0	4.7	5.0
HU	4.3	3.3	3.9
PL	4.1	4.0	4.9
SI	5.1	4.6	4.5
SK	3.0	3.7	3.4
CE	**3.9**	**4.1**	**4.6**
BG	3.7	3.7	3.9
HR	2.6	3.0	3.3
RO	5.7	6.1	8.8
RS	1.1	1.4	2.1
SEE	**4.4**	**4.7**	**6.3**
RU	0.5	2.5	1.8
UA	2.5	2.3	2.1
EE	**0.6**	**2.5**	**1.8**
CEE	**2.2**	**3.3**	**3.3**
TR	5.3	5.4	11.1
DE	2.1	2.3	2.8
EA	**2.1**	**2.4**	**2.6**

Source: Bloomberg, RBI/Raiffeisen RESEARCH

In the second half of 2017 the CEE region again displayed strong growth, leading to further upwards revisions of our estimates for 2017. In Central Europe (CE), average Q3 2017 GDP growth accelerated from 4.1% in Q2 to 4.6% yoy. The Polish, Czech and Slovenian economies steamed forward by growing 4.5-5% compared to the previous year. Hungary and Slovakia were not far behind. In seasonally-adjusted terms though, Q3 growth in CE decelerated slightly to an estimated average of 1.0% after three quarters of growth at levels between 1.2 and 1.3% qoq. **In South-East Europe (SEE)** we are stunned by the continued acceleration of Romania, lifting the regional SEE growth numbers in Q3 to an estimated 6.3% yoy and 2.0% qoq. The CE/SEE region has been supported externally by strong growth dynamics in the euro area (GDP growth of 0.6% qoq in Q3) and especially in Germany. The low interest rates both globally and in many CE/SEE countries are still a positive factor as well. But the rebound in investment, particularly due to higher EU transfers in 2017 and stronger demand in private consumption, boosts growth too. Most recently, the pace of growth has slowed **in Eastern Europe (EE), i.e. Russia, Ukraine**. Nevertheless, comfortable external conditions with regard to oil and metal prices, as well as agricultural products, did support the recovery. Investments and domestic private demand in EE exhibited a notable pickup.

We likewise have strong growth projections in CE/SEE for 2018/2019, further improving the estimate for CE average growth to 3.8% in 2018 and 3.5% in 2019 – both years revised up by 0.5pp. The key change is the more positive view on the Polish economy, which is expected to grow by 4.1% in 2018 and 3.6% in 2019. In the SEE area, aggregate expected growth is slightly lower at 3.7% in 2018 and 3.3% in 2019. The key here is the development of the Romanian economy, which increased by almost 7% in 2017, but should decelerate to a more sustainable 4.2% in 2018. Moreover, it remains to be seen if growth dynamics in the Western Balkans can be sustained (Croatia) or recover (Serbia). In **EE we expect the moderate recovery to continue, with growth of around 1.5% per annum in Russia** and slightly faster in Ukraine at 2.5%-3%. The upcoming Russian presidential elections are not likely to have a strong impact on growth dynamics, while the political risks in Ukraine have to be watched closely. Finally, the Turkish economy is currently booming thanks to domestic stimulus, raising the risks of a sudden cool-down, though our main scenario is a gradual deceleration of GDP growth to around 4% in 2018.

With growth rates in CE/SEE economies having been strong for some time, the previously negative output gaps have likely closed in many markets, or are already slightly positive. In Romania and the CE markets we are already discussing the issue of ongoing or prospective overheating. Looking at the regional labour markets there are signs of upcoming supply-side constraints. Several countries are displaying high nominal wage growth and unemployment rates at multi-year or even historic lows. The CE/SEE economies will thus have to match wage increases with productivity gains in the coming years to avoid weakening their international

competitiveness. **At the same time, the external environment is anticipated to remain growth-supportive:** the German and Austrian economies are expected to grow above their potential in 2018 and 2019 too, while monetary conditions in the euro area should tighten only very tentatively, with interest hikes still several quarters away (first ECB hike expected in Q1 2019).

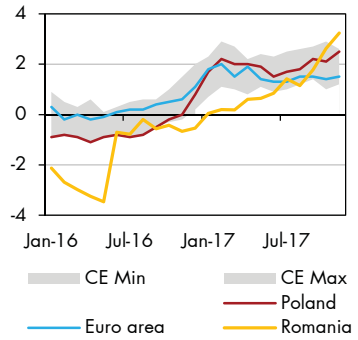
Despite the high wage pressures, inflation dynamics are expected to remain relatively contained – our average CE inflation projections for 2018/19 are only slightly higher than in 2017, at 2.4-2.5%. In Hungary, inflation is expected to amount to 3% in 2018 – the highest in CE. We believe the strongest increase in SEE inflation will be in Romania – to above 4% in 2018, while inflation rates in other SEE markets should remain below 3%. In Russia, inflation fell short of our expectations at below 3%, but it should increase to just above 4% in 2018. Nevertheless, the Russian disinflation story is impressive. In Ukraine and Turkey inflation reached double-digit figures again, but should fall towards the high single digits in 2018.

Monetary policy is set to tighten moderately in several CE/SEE markets during 2018. However, a notable differentiation in the pace of normalisation is emerging. While the Czech monetary policy authorities started in 2017 by exiting the CZK peg and increasing the key rate to 0.5%, the Romanian national bank followed by increasing deposit rates. We expect 3 rate hikes of 25bp in the Czech Republic to 1.25% during 2018, while in Romania the refinancing rate is expected to be increased from Q1 by 125bp overall in 2018. We also expect the Polish authorities will hike rates by 50bp in H2 2018. Notably, the Hungarian authorities (still) see no need to tighten their policies; on the contrary, they continue to add expansionary measures to lower the interest rate at the long end. It is questionable though how long such an ultra-expansionary policy can be maintained for if the environment is increasingly changing. **In Russia, by contrast, interest-rate cuts of at least 100bp towards 7% by end-2018 are expected,** while monetary policy can be loosened in Ukraine again as soon as the inflation rate falls sufficiently (and no further shocks occur).

While **fiscal deficits** in CE (2018: 1.6% of GDP) and in SEE (2018: 2.3% of GDP) should remain well below the 3% Maastricht deficit limit on average, budget deficits in CE and even more so in SEE are expected to deteriorate moderately. As this occurs against a backdrop of strong economic growth with sectoral overheating tendencies (i.e. labour market), fiscal policy is exhibiting a clear pro-cyclical bias that is fuelling business cycle dynamics that are already healthy. Based on European Commission data, the CE and even more so the SEE region continue to have a (sizeable) fiscal impulse in 2018 due to deteriorating fiscal balances in structural terms. At a country level we expect Hungary will record the highest headline fiscal deficits in the CE region until 2019, not least because of the upcoming elections in 2018 (parliamentary) and 2019 (municipal). Having said that, our deficit forecasts of 3.0% of GDP in 2018/2019 are rather conservative. In the SEE region, Romania is the clear negative outlier. Despite high real GDP growth, we expect a deterioration of the headline deficit to 3.5% in 2018. This is not only a sizeable loosening of the fiscal ties, as has already been the case in previous years, but it would also constitute a breach of the 3% Maastricht deficit limit. Consequently, an Excessive Deficit Procedure could be triggered by the European Commission. All in all, CE/SEE governments would be well-advised to pursue a counter-cyclical fiscal policy in order to respond to the overheating tendencies and create more room for manoeuvre during the next economic downturn.

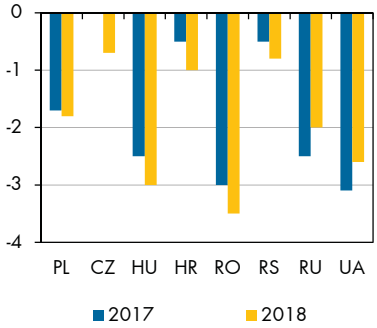
Financial analysts: Andreas Schwabe, CFA, Matthias Reith, CIIA; RBI Vienna

Recent CPI trend (% yoy)



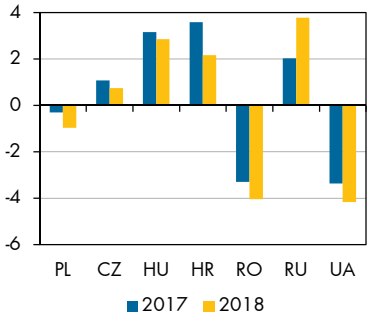
Source: Bloomberg, RBI/Raiffeisen RESEARCH

General budget balances (% of GDP)



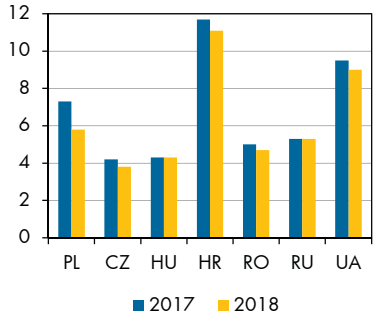
Source: National sources, RBI/Raiffeisen RESEARCH

Current accout balances (% of GDP)



Source: National sources, RBI/Raiffeisen RESEARCH

Unemployment rate (%)

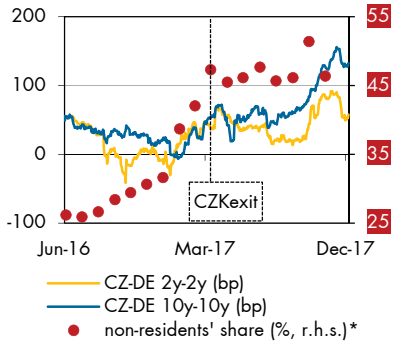


Source: National sources, RBI/Raiffeisen RESEARCH

Emerging European debt markets dominated by FX returns next year

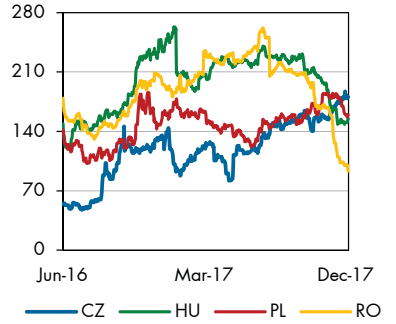
- **Seesaw on CZGB market to continue; CZGBs as a vehicle to express constructive CZK view**
- **Favourable PLN expectations brighten Polish debt market outlook, especially should EU tensions ease**
- **Short-term performance outlook for rouble government bonds favourable, FX risks to weigh later-on, though**
- **Turkish LCY debt market only a tactical Buy for the boldest yield hunters due fragile TRY prospects**

CZGB spreads vs Bunds and NRH*



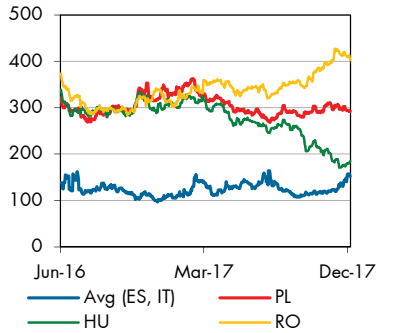
** % share of non-resident holdings (NRH) in total CZK government bonds (CZGBs) outstanding*
2y-2y: 5y high 92 5y low -42
10y-10y: 5y high 156 5y low -23
Source: Bloomberg, MinFin, RBI/Raiffeisen RESEARCH

ROMGB & HGB curve flattening



**10y minus 2y local currency (LCY) yield (bp)*
CZ: 5y high 243 5y low 33
HU: 5y high 263 5y low 12
PL: 5y high 186 5y low 45
RO: 5y high 262 5y low -2.6
Source: Bloomberg, RBI/Raiffeisen RESEARCH

10y yield spread vs Bund*



** 10y LCY yield spread over 10y Bund in bp*
Avg (ES, IT) 5y high 583 5y low 89
PL 5y high 363 5y low 161
HU 5y high 514 5y low 171
RO 5y high 540 5y low 226
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Czech Republic: Seesaw to continue: strategic Hold / tactical Buy

Since our last CEE Strategy publication on 21 September and 14 December (cut-off date for data of this report), CZGBs have underperformed in absolute LCY terms – despite the 1.5% CZK appreciation vs EUR. The long-end of the curve posted more losses than the short, with the 10y-10y spread vs DE widening by some 50bp in the observed period (driven almost exclusively by CZGBs). Reaching a new record high of 51% as of September, non-resident holdings (NRH) declined to 46% in Oct, which means almost no change vs 6 April ('CZKexit'). Despite 5% CZK appreciation vs EUR since CZK re-floating, the 2y CZGB has gained 1% since then, while the 10y benchmark government bond lost 1.3% (in absolute, LCY terms). Of course, while there were many profit-takers amongst NRs, there were at least the same number of buyers following the spread normalisation mentioned above. This makes sense since the long-term CZK appreciation trend is still intact given its considerable undervaluation in fundamental terms. We expect a gradual CZK strengthening in H1 2018 amidst yields inching upwards, the latter driven by continued but cautious rate hikes. Hence the seesaw on the CZK debt market is expected to continue with FX gains probably overcompensating the price losses slightly. Positioning risks remain elevated in any case since faster than anticipated FX gains could essentially trigger massive profit-taking. We would pencil-in this risk via a projected setback in CZK vs EUR in H2 2018.

Hungary: Can the MNB really keep the long-end under control? Hold

The MNB currently enjoys great authority vis-á-vis market participants as the two additional unconventional MP measures – announced in November – have already delivered the desired primary effect. Apart from HUF weakening, the explicit goal of policymakers is to bring fixed-rate mortgage loan rates down by depressing long-end HGB yields. While the government immediately benefits from sinking refinancing costs, the benefits for mortgage loan takers will take time. However, starting from Jan 2018, 5y and 10y IRS tenders amounting to HUF 1.0-1.5 tn for 2018 will be introduced. The second measure is outright MBS buying. The targeted amount is more than half of the outstanding securities, i.e. > HUF 500 bn. Given that the currently tight HGB valuations should already widely reflect the additional easing measures, the room for further yield declines appears limited. Despite the massive flattening recently, the HGB curve has still a slope roughly in line with peers. Over a longer-term horizon we expect a more or less flat HGB performance with a growing inflation premium likely to eat into the total performance. The major risk to our neutral HGB recommendation stems from faster-than-expected core bond yield normalisation. At the same time, the external vulnerability of HGBs is steadily sinking due to the ongoing decline in non-resident holdings, which are obviously well absorbed by local investors.

Poland: Slight overweight due to assumption of moderating EU conflict

The ongoing dispute with the EU focused on the judiciary reform is the main reason that Polish bonds have not posted an even better performance. Nevertheless, between 21 September and 14 December 10y POLGBs gained more than 2%, bringing YTD gains to more than 7% in absolute, LCY terms. The combination of robust economic growth, moderate inflation, and neutral MP provide a beneficial fundamental environment for PLN bonds. But: CPI headline growth is expected to accelerate and finally push the Polish MPC towards a more hawkish stance (MP lift-off expected for Q3 2018). The related upward pressure on POLGB yields and the rising core market pressure should turn out as moderate, though. We believe that the recent government reshuffling is basically brightening the prospects for the resolution of the controversial issues with the EU. However, too much gains should not be expected, which should be anyhow mainly driven by the FX component.

Romania: Hold, thanks to the attractive carry

In the first two weeks of December, ROMGBs were in relief mode. The 10y tenor outperformed the RON curve, gaining 2%, which reduced YTD losses in this segment to 8%. Some slightly better news on the fiscal front was definitely supportive for the rally. In addition, the BNR started to take a more active part in tackling economic overheating risks. Due to the stronger-than-expected underlying inflationary pressures, we upped our rate hike forecasts markedly for 2018, adding two 25bp hikes to the earlier three. However, the short-term prospects for ROMGBs appear rather neutral, mainly due to the still elevated yield advantage that is likely counterbalancing the potential price losses. Risks will remain elevated though if government policies become more fickle again.

Russia: Buy, since RUB depreciation is likely to materialise only in H2 2018

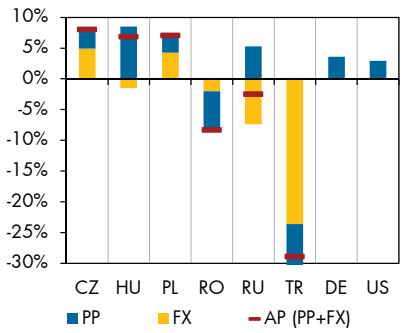
Given our call for slightly stronger USD vs the EUR, EUR-based OFZ market investors in particular could post moderate gains on our end-Q1 2018 recommendation horizon. Especially short-dated OFZs have potential due to deeper than earlier expected rate cuts. The long-term outlook is clouded though since significant RUB weakening is expected that should easily erase the expected price gains. Although rate cuts could become deeper than initially expected, the CBR should not overdo them and, in addition, much of this is already priced in to RUB bonds. Finally: we do not expect that sanctions will be extended on the OFZ market.

Turkey: Tactical Buy once TRY currency starts temporary appreciation

Turkish rate-setters disappointed market participants on 14 December raising the late liquidity window (LLW) by only 50bp versus the 100bp consensus expectations. As we have repeatedly stated, we would only re-enter TURKGBs in the event of a significant improvement in FX outlook. If the TCMB were to use the LLW exclusively, the weighted average costs of funding (WACF) would only increase to 12.75% from the current 12.25%. We reckon the central bank is playing on the expected start of a significant disinflation process, which would turn real yields positive in Q1 2018. As we think this strategy has a good chance of working out, we expect renewed TRY relief in Q1, also triggering TURKGB gains. However, we do highlight the highly speculative nature of this recommendation.

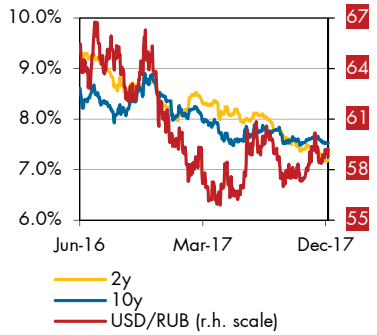
Financial analyst: Stephan Imre, RBI Vienna

Year-to-date performance 10y LCY bond*



** absolute performance of 10y LCY bond in LCY year-to-date (until 14 Dec 2017)*
FX: Currency performance (chg EUR/LCY)
PP: Bond price performance (price chg + carry)
AP: Absolute performance (PP + FX)
Source: Bloomberg, RBI/Raiffeisen RESEARCH

OFZs co-move with RUB*

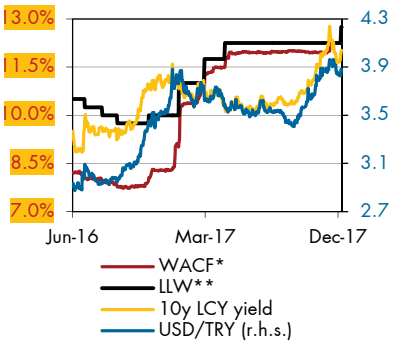


** 2y and 10y LCY yields vs USD/RUB*

2y:	*5y high*	*17.5*	*5y low*	*5.7*
10y:	*5y high*	*16.1*	*5y low*	*6.5*
USD/RUB:	*5y high*	*82.3*	*5y low*	*29.9*

Source: Bloomberg, RBI/Raiffeisen RESEARCH

MonPol tight enough?*



** weighted average costs of funding*
*** late liquidity window*

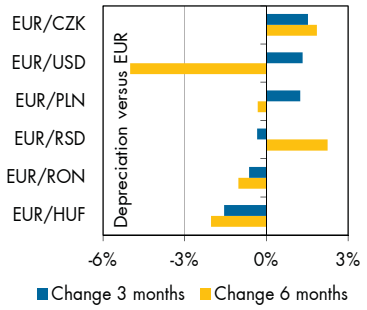
WACF:	*5y high*	*12.3*	*5y low*	*4.5*
LLW:	*5y high*	*15.0*	*5y low*	*9.5*
10y yield	*5y high*	*12.8*	*5y low*	*9.5*
USD/TRY	*5y high*	*4.0*	*5y low*	*1.7*

Source: Bloomberg, RBI/Raiffeisen RESEARCH

CZK and PLN strengthening potential not yet exhausted

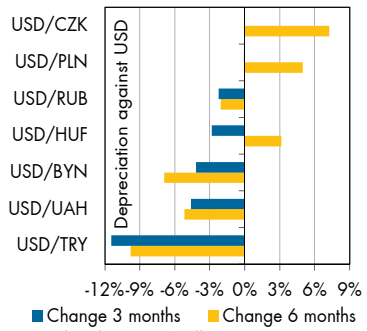
- **Expectation of ongoing appreciation in CZK and PLN during Q1**
- **Despite positive economic conditions, politics still main burden for numerous CEE currencies**
- **Russian rouble seen to be weaker over course of 2018, especially versus EUR in H2**
- **Political risk the main burden for TRY, no sustainable recovery expected**

Change of LCY value to EUR (%)



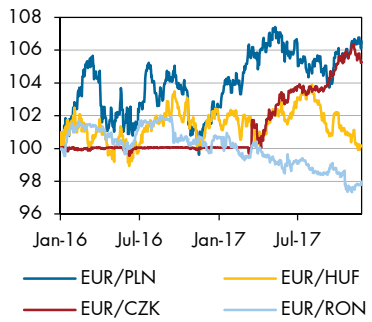
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Change of LCY value to USD (%)



Source: Bloomberg, RBI/Raiffeisen RESEARCH

Currency comparison*



** indexed chart: January 2016 = 100*
Source: Bloomberg, RBI/Raiffeisen RESEARCH

The fourth quarter of 2017 saw some deviations in development within the CEE region. While the CE currencies mostly strengthened against the EUR, the SEE currencies witnessed a slightly negative to flat development. EE currencies performed negatively both against the euro as well as the USD.

One high flyer in Q4 – as predicted – **was the Czech koruna** against the euro, continuing to appreciate after abandoning the FX regime in April. The other strong performer was the Polish zloty that likewise appreciated as predicted, but here, our forecast of elevated volatility did not materialise the way we had expected. The Hungarian forint, on the other hand, trended slightly negative against the euro over the fourth quarter.

Our sell recommendation for the Serbian dinar was not a total success as the RSD merely lost 0.5% versus the euro in the course of Q4 2017 – somewhat less than we had projected. The hold recommendation on the remaining SEE currencies on the other hand worked out well, as the movement against the euro was subdued. The Romanian leu remained at elevated levels as expected with the prolonged risk of economic imbalances.

In the **EE region the forecasted RUB stability worked out very well** over the fourth quarter with the USD/RUB trading around our projection of 58. The expected UAH depreciation towards 27 against the USD also proved correct. The BYN, on the other hand, witnessed a more pronounced depreciation trend than we had already anticipated.

The **most difficult projection though was the Turkish lira.** Despite the TRY already being massively undervalued, politics generated additional depreciation pressure for large parts of Q4. Here, our hope for any stabilisation or even a recovery was premature, while at the same time supporting our view not to have TRY as a buy recommendation for Q4.

The upcoming first quarter in 2018 is set to bring additional appreciation potential for some CE currencies. Both the **CZK and PLN are forecasted to appreciate** against the euro: the koruna due to a continuation of the rate-hiking cycle and the persistent undervaluation after the "CZKexit", and the zloty thanks to strong economics and the recurring rate-hike speculation. We therefore give a buy recommendation for both, while preferring the CZK over the PLN given the lingering political risks in Poland. The Hungarian forint, on the other hand, should continue trending sidewards around levels of 310-315 to the euro.

In the SEE region we predict a moderate strengthening for the Croatian kuna due to seasonal trends. For the Romanian leu we only predict a sideways movement around EUR/RON 4.65-4.70, despite the upcoming interest-rate hikes, in light of the residual risk of economic imbalances. Both the Albanian lek as well as the Serbian dinar should witness very moderate depreciation against the euro, but not enough to justify a sell recommendation in our view.

The **Russian rouble** as the heavyweight currency in the EE region is predicted to undergo (moderate) **depreciation over the coming months against the USD**,

albeit not to an extent that would indicate a sell recommendation for Q1 2018. The declining carry with ongoing key rate cuts, sluggish economic growth or the new budget rule that diminishes the rouble correlation with the oil price are among the topics supporting such a moderate depreciation trend. Against the euro the RUB should witness some appreciation potential for Q1 2018, but this is mostly due to our EUR/USD assumptions and not due to any rouble related topics. For the Ukrainian hryvnia we likewise see some potential for a slight setback against the USD in Q1 with risks stemming from the political side. The Belarusian rouble should continue its basic depreciation trend, whereby the magnitude of this depreciation should by and large follow the Russian rouble.

The toughest cookie for the first quarter in 2018 should once again be the Turkish lira. On the negative side we have ongoing political risks, high indebtedness in USD, elevated inflation and the question of how much political influence there is on the monetary policy decisions by the Turkish Central Bank. On the positive side, we have the already significant undervaluation of the lira, possible support by the central bank, strong economic growth and the expectation of declining inflation rates in Q1 due to base effects. All in all we have to stress that any prediction about TRY movements currently comes with elevated risks. Nevertheless, we at least see some TRY recovery potential for Q1 given the oversold nature of the lira, the expectation of declining inflation and the lingering speculation about central-bank measures. But again, we refrain from making any buy recommendation, especially for an end-of-period perspective.

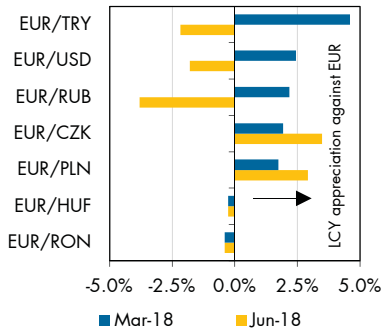
On a **one-year horizon we can only see the CZK strengthening against the euro.** For the PLN we expect a setback in H2 that translates into a sidewards movement over a 12-month horizon against the euro, while the Hungarian forint is expected to exhibit moderate depreciation against a stronger EUR. This hinges to a large extent on the end to the ECB bond-buying program and indications by the ECB on upcoming key rate hikes, while at the same time the Hungarian Central Bank (MNB) should stick by its very expansive monetary policy for longer. The currencies of the SEE region should likewise experience moderate declines versus a strengthening euro over the course of the next 12 months.

The stronger euro exerts a notable effect on the EE region especially. While we already predict EE currencies will weaken against the USD, especially during H2 2018, the EUR/USD effect should amplify this effect. As a consequence we forecast RUB depreciation versus the euro of roughly 15% until eop 2018; the same figure for UAH should be around 10%.

Making any 12-month outlook for the Turkish lira is extremely difficult. Without a pronounced central bank reaction and a calming of the political noise, we would expect continued depreciation pressure to persist overall. We currently project some recovery potential for Q1, but remain pessimistic for the remainder of the year.

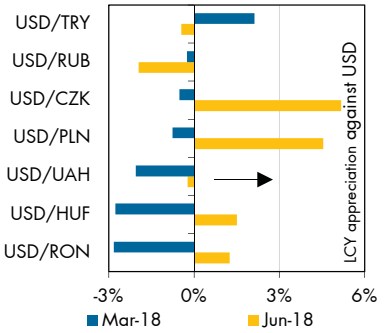
Financial analyst: Wolfgang Ernst, CEFA, RBI Vienna

Projections LCY vs EUR



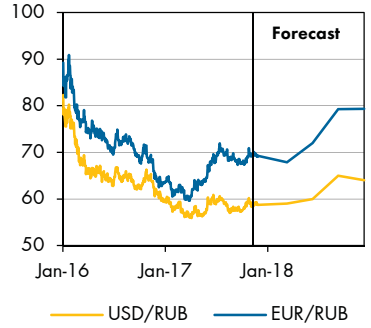
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Projections LCY vs USD



Source: Bloomberg, RBI/Raiffeisen RESEARCH

RUB setback projected for 2018



Source: Bloomberg, RBI/Raiffeisen RESEARCH

Embracing the reality of lower returns likely in Q1 2018

- **CEE still managed to produce the second-best EM result with a +0.6% gain in Q4**
- **Positive re-rating story to continue into 2018 with CE in the lead and SEE slowly catching up**
- **EM risk profile less stable as rising costs of borrowing may exert pressure on economies**
- **Inside CEE we recommend a tactical Hold on the majority of CEE**

EMBIG USD index & spreads[1)]

	14-Dec			Spread value, bp	
	Index	Spread, bp	qoq[1)]	5y min	5y max
LT (A-)	181	34	-19	28	232
PL (BBB+)	639	48	-9	44	180
RO (BBB-)	164	122	-8	114	313
HU (BBB-)	331	97	-5	92	424
KZ (BBB-)	219	200	-29	195	544
TR[1)] (BB+)	759	306	18	170	390
RU (BB+)	1137	189	-2	152	702
HR (BB)	171	113	-17	110	402
RS (BB-)	249	110	-22	104	488
BY (B)	104	344	2	314	1747
UA (B-)	802	461	-11	438	4281
Europe[1)]	1215	237	7	-232	456
Africa	1069	336	-29	239	714
Asia	676	161	2	148	304
Mid East	536	402	24	336	602
Latam	718	421	18	297	719
Global	**806**	**318**	**11**	**244**	**532**
Inv.grade	**601**	**183**	**4**	**146**	**337**
BB	**794**	**253**	**6**	**188**	**457**
B	**1343**	**387**	**-10**	**377**	**995**

1) 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[1)]	Direction[2)]
CE:		
CZ	AA-(s) / A1(s) / A+(p)	⇔⇧
SK	A+(s) / A2(p) / A+(s)	⇔⇧
PL	BBB+(s) / A2(s) / A-(s)	⇔
LT	A-(p) / A3(s) / A-(s)	⇔⇧
LV	A-(p) / A3(s) / A-(s)	⇔⇧
SI	A+(s) / Baa1(s) / A-(s)	⇔⇧
HU	BBB-(p) / Baa3(s) / BBB-(p)	⇧
SEE:		
RO	BBB-(s) / Baa3(s) / BBB-(s)	⇔
BG	BBB-(s) / Baa2(s) / BBB(s)	⇔
TR*	BBu(n) / Ba1(n) / BB+(s)	⇔⇩
HR	BB(p) / Ba2(s) / BB(s)	⇔⇧
RS	BB-(p) / Ba3(s) / BB-(s)	⇔⇧
AL	B+(s) / B1(s) / n.r.(*)	⇔
BH	B(s) / B3(s) / n.r.(*)	⇔
EE:		
KZ	BBB-(s) / Baa3(s) / BBB(s)	⇔
RU	BB+(p) / Ba1(s) / BBB-(p)	⇔⇧
BY	B(s) / Caa1(s) / B-(p)	⇔⇧
UA	B-(s) / Caa2(p) / B-(s)	⇔

⇔ no change, ⇧ upgrade possible, ⇩ downgrade possible; 1) rating - S&P/Moody's/Fitch, Turkey S&P unsolicited rating; 2) the likelihood of rating change in 3 to 12 months; Source: Rating agencies, RBI/ Raiffeisen RESEARCH

Market trends and ratings

The outgoing quarter was characterised by significant swings of Eurobond spreads amidst rising 10y UST volatility. In October this situation detracted slightly from the positive performance of the majority of CEE, excluding only Georgia and Ukraine. Still, a falling correlation between UST and EMBIG allowed CEE to boost its performance from late November, as opposed to the tame results of October. The **tightly-priced CEE still managed to produce the second-best EM result with a +0.6% gain in Q4,** falling behind only Africa EMBIG and outstripping the Composite index by 0.5%. Our bets on Kazakhstan and Ukraine made back in September delivered above-average returns of 3.3% and 1.4% respectively, while Turkey very much underperformed our targets. Overall the Q4 result was positive for CEE, with risk-taking still favouring the higher-yielding EE and Romania. The technical picture remained relatively balanced for CE and SEE as compared to a year ago, while the larger jump in EE issuances can be explained by overly low volumes initially in preceding years.

The rating picture has brightened up throughout 2017 with a number of positive outlooks and upgrades strongly outnumbering the negative rating actions. In fact, the positive outlook balance reached +12, with 14 positive vs only 2 negative outlooks for Turkey, while the recent upgrade of Bulgaria by Fitch and S&P reduced the positive outlook balance back to +10. We remain especially optimistic on CE, which holds half of all the positive outlooks in the region. Hungary, Latvia and Lithuania have the strongest chances of seeing their ratings rise by one notch, while the likelihood of a rating upgrade is also greater for the Czech Republic and Slovakia. In SEE, Croatia and Serbia are likely to be front-running candidates for a one-notch rating upgrade, while in EE the best chances may still lie with Russia and Belarus. In Russia we are a little cautious because of new US sanctions potentially delaying, but not cancelling, an otherwise imminent one-notch upgrade. On the other hand, our earlier conviction about a one-notch upgrade for Ukraine has weakened considerably due to the worsening reform outlook and political instability. Altogether we project the **positive re-rating story will continue into 2018, with CE remaining in the lead and SEE slowly catching up.** The only two negative stories so far will be Turkey, where politics is suppressing the outlook, and Romania, where fiscal loosening is likely to put outlooks under pressure in 2018.

Primary markets

Primary market activity was logically down in Q4 as the majority of CEE sovereigns managed to pre-fund their yearly borrowing programs for 2017, and a few were even looking to start pre-funding their 2018 needs. The most interesting placements included the return of Hungary, with a EUR 1 bn issue, and Croatia, with a EUR 1.3 bn program, both tightly priced amidst high demand. In 2018 we project similarly strong activity, especially as domestic market yields will continue rising in a number of CEE countries, thus pushing them towards the Eurobond market for

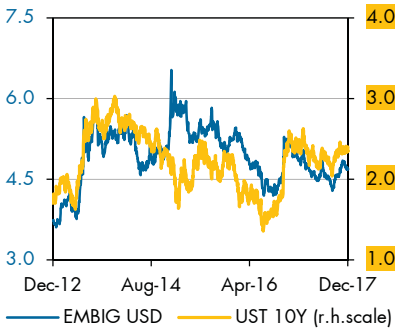
cheaper funding. As a result we estimate CEE sovereign placements will total USD 32-38 bn in 2018, accounting for lower issuance activity from Russia with no debt swap plan for next year.

Outlook and strategy

Although the flattening of the UST curve and the already wide 10y UST yield price in the forthcoming Fed rate hikes could imply a slower yield increase going forward, we identify the smaller response from EM Eurobonds in the past as a risk factor. Indeed, the **relatively low yields in developed markets (DM) prompted investors to remain in higher-yielding EM debt for longer**, as the alternatives, especially in the euro area, remain scarce. Nevertheless, as the policy-tightening bias progresses we predict more negative headwinds for EM. Firstly, the correlations between rising yields on DM and EM will strengthen again once the next rate move is priced in, so even flat spreads still imply rising yields. Secondly, the EM risk profile is becoming less stable as the rising costs of borrowing will exert pressure on economies too. Geopolitical tensions also influence the outlook in the case of countries like Russia. In this environment we would expect a gradual spread increase for nearly all CEE sovereigns, while weaker EE countries and Turkey could come at a bigger risk. Taking a global perspective, CEE has the tightest valuations among all EM except Asia. With the CEE aggregate EMBIG USD spread hitting close to 130bp, the risk of a market correction is increasing. Inside **CEE we tactically recommend a Hold (neutral) position on the majority of CEE.** We downgrade Ukraine from Buy to Hold on the back of its worsening political situation and failing reforms, which raise issues with the IMF and EU. We also downgrade Turkey from Buy to Hold on the political uncertainty negatively impacting its risk premia. Last but not least, Poland and Lithuania remain on a tactical sell due to their overly tight valuations.

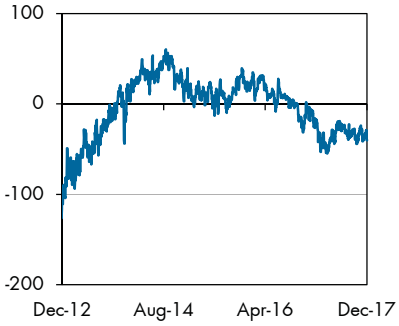
Financial analyst: Gintaras Shlizhyus, RBI Vienna

CEE EMBIG vs UST 10y yields, %*



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

CE/SEE vs EUP spread (bp)*



** spread in basis points between CE/SEE yield (duration adjusted) and 5y EU Peripheral (EUP) average yield, 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

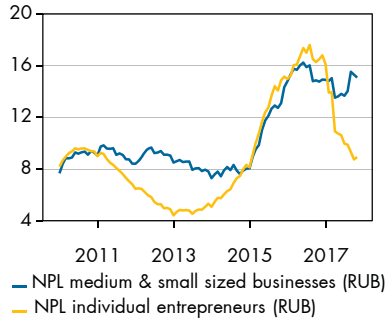
				Spread		Range			Spread	Range			Spread	Range		
Issue		Rating	Dur.	14-Dec	Mar-18	min.	max.	Perf. (%)	Jun-18	min.	max.	Perf. (%)	Sep-18	min.	max.	Perf. (%)
LT 6.625% due 22	USD	A-	3.6	**28**	**35**	32	38	-0.7	**40**	36	43	-1.8	**45**	42	49	-2.4
LT 2.125% due 26	EUR	A-	8.3	**73**	**80**	77	83	-0.9	**88**	85	90	-1.5	**101**	98	103	-3.0
PL 3% due 23	USD	BBB+	4.8	**42**	**50**	46	54	-0.8	**56**	52	61	-2.5	**65**	60	69	-3.4
PL 0.875% due 27	EUR	BBB+	9.1	**100**	**95**	93	97	-1.0	**104**	102	106	-4.8	**119**	117	121	-6.2
RO 4.375% due 23	USD	BBB-	5.0	**80**	**90**	84	96	-0.9	**100**	94	106	-2.9	**115**	110	121	-4.2
RO 2.75% due 25	EUR	BBB-	7.2	**155**	**160**	156	164	-1.4	**175**	171	179	-4.0	**201**	197	205	-7.3
HU 5.375% due 23	USD	BBB-	4.5	**78**	**80**	73	87	-0.6	**90**	83	98	-2.3	**104**	97	112	-3.4
HU 3.875% due 20	EUR	BBB-	2.1	**64**	**70**	66	77	-0.5	**79**	76	86	-1.1	**93**	89	100	-1.8
BG 2.625% due 27	EUR	BBB-	8.4	**112**	**110**	106	117	-1.1	**123**	119	130	-1.2	**143**	139	150	-3.3
TR 3.25% due 23	USD*	BB+	4.7	**229**	**220**	206	234	0.0	**245**	231	260	-2.6	**282**	268	296	-4.8
TR 4.125% due 23	EUR*	BB+	4.7	**283**	**270**	266	278	-0.1	**296**	292	303	-2.3	**342**	338	349	-5.4
RU 4.5% due 22	USD	BB+	3.9	**82**	**80**	69	91	-0.4	**92**	81	103	-1.9	**106**	95	117	-2.8
HR 5.5% due 23	USD	BB	4.6	**119**	**120**	105	135	-0.6	**138**	123	153	-2.7	**159**	143	174	-4.1
HR 3% due 25	EUR	BB	6.5	**188**	**180**	171	197	-0.5	**204**	195	221	-4.2	**238**	229	255	-6.4
RS 7.25% due 21	USD	BB-	3.3	**101**	**120**	111	129	-1.0	**134**	126	143	-1.8	**154**	146	163	-2.8
BY 7.625% due 27	USD	B	6.7	**374**	**375**	335	415	-0.4	**427**	387	467	-5.2	**448**	408	488	-7.3
UA 7.75% due 27	USD	B-	6.7	**490**	**510**	476	544	-1.9	**569**	535	604	-7.9	**558**	524	592	-7.8

** 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

Russian corporate Eurobonds remain popular

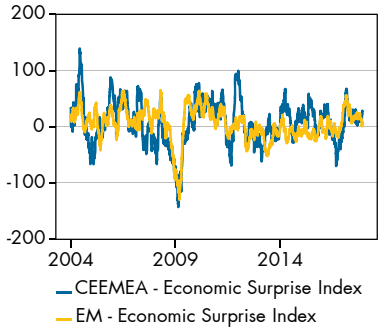
- **Low volatility for Russian corporate Eurobonds in the past period**
- **Positive development of oil prices bolsters support for expensive valuations**
- **Economic conditions remain benign for creditors**

RU - Non-performing loans (in %)



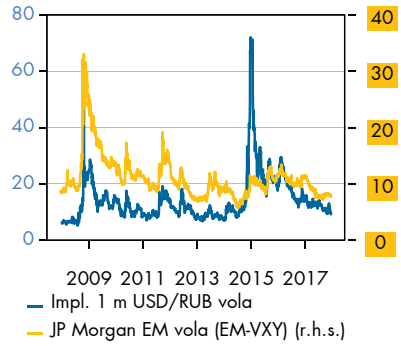
Source: CBR, Bloomberg, RBI/Raiffeisen RESEARCH

EM - Economic surprise indices



Source: Citi, Bloomberg, RBI/Raiffeisen RESEARCH

Impl. USD/RUB vola vs JPM EM vola*



** in %*

Source: Bloomberg, RBI/Raiffeisen RESEARCH

Developments in risk premiums on the Emerging Market (EM) credit markets were relatively varied compared to each other during the course of the year. Nevertheless, all of the markets (Latin America, Eastern Europe, Africa) were mainly influenced by the declines in spreads on the established markets. Furthermore, the **elevated risk aversion** seen on the high yield credit markets in the euro area and the USA **starting from end-October 2017** was not felt on all of the EM credit markets. First and foremost, this included the **Russian corporate Eurobond market**, which remained **almost completely unscathed by the setbacks**, despite featuring relatively high valuations in our opinion. We mainly ascribe this to the fact that the Russian corporate sector is disproportionately dependent on the oil price trend, and this trend has not flattened out in the autumn and winter months. At the same time, there was a modest decoupling of the RUB/USD exchange rate from the oil price developments. RUB did not appreciate versus USD as strongly as the development of oil prices in the past months would have suggested, and this had positive effects on Russia's oil-exporting corporate sector.

Fundamental economic conditions look **quite benign for creditors in Russia and in the Eastern European region**. Although the regionally-specific Economic Surprise indices signalled slightly less positive surprise momentum in the past period, most of the economic indicators have still surpassed analysts' expectations since the beginning of the year. For example, the fundamental performance of the portion of the corporate sector which is not oriented towards oil prices is supported by solid developments in retail sales and car sales, and consumer confidence is heading back towards the strong levels from 2013–2014.

On a negative note, the positive trend in industrial production did not continue and new construction activity and investment in new production capacities is practically stagnant. The reason for this may be that the credit growth of the non-financial sector is considerably weaker than household credit growth in year-on-year terms (leading to **positive economic indicators in relation to households, but weaker performance for indicators which are more directly related to the corporate sector)**. Our economic experts for Russia project growth of between 1.5% and 2% next year in Russia, with expectations of a continued recovery in private consumption and rising investment activity on the order of four percent.
In our view, the biggest risk for a correction on the Russian corporate Eurobond market is a major setback for the oil price and the extremely expensive valuations (regardless of what model or basis for comparison one uses) versus risk-equivalent EM credit markets. Sooner or later, this could lead to reallocation of creditors' funds. At the moment, we see the likelihood of either of these factors materialising as being extremely low, and consequently we expect to see **sideways movement in spreads on the Russian credit market in the quarter ahead**.

Financial analyst: Christoph Klaper, CFA; RBI Vienna

The **technical situation remains largely benign** in our view as many Russian corporate credits can afford to deleverage amidst adequate liquidity buffers and comfortable free cashflows.

Still, the **net supply of Russian corporate Eurobonds is expected to remain negative amidst the sanctions regime.**

The **sanctions topic will also remain on the radar** in the coming months. To recap, after the June vote by the US Senate to expand the sanctions on Russia, they were transformed in August from an executive order at the discretion of the White House to a federal law, which requires a congressional majority to be changed. That makes it **harder to lift the sanctions currently imposed** in our view. Clearly the sanctions remain a risk factor for some credits as the new law enables the US President to expand them to ban the development of Russian pipeline projects (specifically Nord Stream 2). We will be keeping an eye out for the **February 2018 deadline when the new US legislation** is likely to be passed including fresh (personal) sanctions against Russia. We also note that certain measures are being taken by the Russian government to protect domestic banks from new punitive curbs related to the financing of the defence industry.

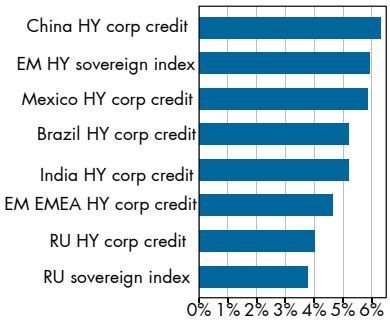
In **the Russian banking sector, we expect further stabilisation** after the stormy autumn days, which may reopen the primary market for private names. In our recommendations we stick with only strong idiosyncratic stories in the AT1/AT2 asset class and SIFI profiles concerning the senior unsecured rank. In particular, we like the CRBKMO 8.875% perpetual as the bank has demonstrated a resilient operating performance, an ability to raise capital on the stressed market via an SPO (USD 250 mn) and extra subordinated deposits from large corporate clients (USD 370 bn). Among the state-related names, on the back of strong government support we recognise VEB as an attractive offer in the quasi-sovereigns league, where we recently issued a **buy call for VEBBNK 6.902% due 2020 (USD) and VEBBNK 4.032% due 2023 (EUR)**. We also continue favouring the strong fundamental story of Sberbank, having **its SBERRU 6.125% due 2022 on buy.**

Turning to other sectoral views we expect an **improved outlook for the steel sector**. According to the World Steel Association, Russia's domestic steel demand should grow by 2.3% and 3.2% in 2017 and 2018 respectively, after the declines in 2016 and 2015 of -3.6% and -8.3% respectively.

Furthermore, we believe that **higher cash costs due to RUB strengthening vs the USD will be largely offset by the firmer pricing environment and a healthy recovery in domestic and external demand.** On a separate note, the anti-dumping duties imposed on Russian producers by the EU and the US have so far only had a negligible impact due to the rather narrow range of products affected (flat steel) and the ability of producers to refocus on other products. However, the question remains to what extent the list of banned products will remain the same or will be expanded, which would imply a greater threat for the top lines of Russian steel producers. We maintain our **buy recommendation on EVRAZ 5.375% due 2023.**

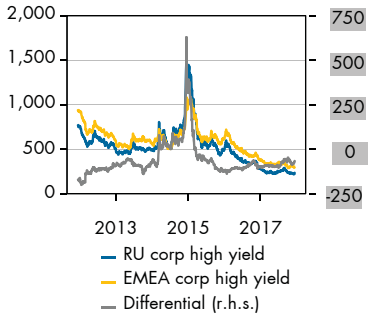
Financial analysts: Martin Kutny, CFA, Ruslan Gadeev; RBI Vienna

EM Yields in comparison (in %)



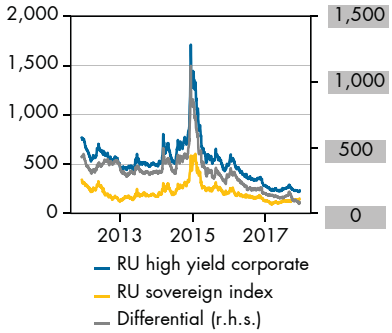
Source: ICE Bank of America Merrill Lynch, RBI/ Raiffeisen RESEARCH

RU HY corp vs EMEA HY corp spreads *



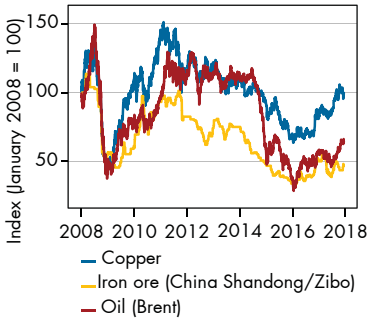
** OAS in bp*
Source: ICE Merrill Lynch, RBI/Raiffeisen RESEARCH

RU HY corp vs RU sovereign index*



** OAS in bp*
Source: ICE Merrill Lynch, RBI/Raiffeisen RESEARCH

Commodity prices (indexed)

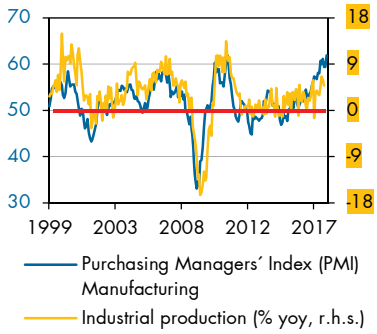


Source: Bloomberg, RBI/Raiffeisen RESEARCH

Robust upswing generates strongest growth seen in the last 10 years

- **Economic activity remained vibrant in the third quarter, driven by both domestic demand and foreign trade**
- **Strong cyclical development of equipment investment has probably peaked out**
- **2017 GDP growth revised up from 2.8% to 3.2%, marking the highest rate of growth since 2007**
- **Nevertheless, fully utilised production capacities no longer reflect any need to "catch up"**

Sentiment: "hard" slowly catching up

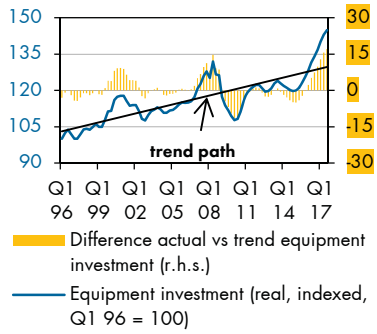


Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

During the third quarter of 2017, the economic upturn in Austria continued full speed ahead, as real GDP expanded at a rate of 0.9% qoq (Wifo trend business cycle component), which corresponds to the average rate recorded for the first half of the year. In all three quarters of 2017, **economic activity was driven by domestic demand and net exports**. The positive development of private consumption which started in 2016 continued in 2017. However, whereas the key supporting factor in 2016 was the tax reform which entered into force early in the year, the acceleration in employment was the driving force in 2017. Equipment investment has continued to increase strongly, but has probably already passed its peak. By contrast, growth in construction investment weakened somewhat in the second and third quarter, following a vigorous start to the year.

The outlook for the coming months still looks positive. For instance, the **purchasing managers' index for the manufacturing sector** is currently at its **all-time high** (61.9 points), which it last reached in February 2011. Based on the current levels, this means that there is **limited potential for any more substantial improvement in sentiment**. That said, sentiment is still overstating actual economic conditions, and consequently any (moderate) decline in the aforementioned and others indicators would merely represent a convergence to current conditions.

Investment cycle already mature



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

The main reasons for our **raised GDP forecasts** for 2017 and 2018 are the performance of the economy during the first three quarters of 2017 and the positive outlook going forward. As such, we now forecast that **real GDP will expand by 3.2% in 2017 (previously 2.8%)**, which is mainly owed to better than initially expected business cycle dynamics in the first three quarters of 2017 (the quarterly growth rates for Q1–Q3 were revised upwards upon publication of the final GDP figures for Q3 on 30 November). The upward revision of the **GDP forecast for 2018 (from 2.2% to 2.6%)** is based on the resulting statistical overhang and the sustained, positive outlook. Consequently, in 2017 Austria should record the highest GDP growth since 2007 and be one of the leading

Key economic figures and forecasts

	2016	2017e	2018f	2019f
Real GDP (% yoy)	1.5	3.2	2.6	1.6
Trade balance (goods and services, EUR bn)	11.9	14.5	17.2	18.9
Current account balance (% of GDP)	2.1	1.7	1.7	1.5
General budget balance (% of GDP)	-1.6	-0.7	-0.7	-0.6
Public debt (% of GDP)	83.6	77.9	75.1	72.8
Unemployment rate (avg, %, EU definition)	6.0	5.5	5.3	5.2
Employment (% yoy)	1.5	1.9	1.6	1.2
Consumer prices (avg, % yoy)	1.0	2.2	2.1	2.1
Real wages (% yoy)	0.6	-0.7	0.6	0.6
Unit labour costs (% yoy)	2.1	0.2	1.7	2.3

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

countries in this regard in the euro area. That said, **business cycle dynamics are forecasted to moderate over the forecast horizon** (2019: 1.6% yoy, previously: 1.4% yoy). Because as the output gap has already been closed, even the projected moderation of growth rates would cause a degree of overutilization of capacities which was previously seen only during the peaks of the last two cyclical upturns (2007/2008 and 2000).

In **2018 and 2019, business cycle dynamics should continue to be borne by both domestic demand and net exports**. Relatively stable growth contributions are expected from **private consumption** due to further improving labour market conditions and rising consumer confidence, which should be reflected in a modest drop in the savings rate. By contrast, growth in **gross fixed capital formation** should slow down considerably, due in large part to developments in equipment investment. Construction investment, on the other hand, should benefit from still favourable financing conditions, rising real estate prices, and robust, sustained demand thanks to population growth. In line with business cycle dynamics of Austria's key trading partners (euro area, CE/SEE), **export** growth is expected to slow down as well. However, as the same should hold true for import growth, net exports are likely to continue yielding positive growth contributions until 2019.

The **labour market** is assumed to remain a reflection of healthy business cycle dynamics. Employment growth is around 2% yoy, with the manufacturing sector as the main driving force behind this. The positive trend should continue in 2018 and 2019, although a slower pace of employment growth is anticipated, in line with the development of the overall economy. In 2017, the average unemployment rate (ILO definition) will decline for the first time since 2011. In 2018 and 2019, however, the rate of unemployment is only expected to decline moderately.

Inflation (HICP) ran at 2.2% yoy in the first ten months of the year, compared to 1.0% on average for 2016. Most of the increase stemmed from oil price developments, along with food prices. For 2017 as a whole, we project an inflation rate of 2.2% yoy. Following a mild decline at the start of the year, inflation should accelerate again as 2018 progresses and reach a level of 2.1% for the year as a whole (2019: 2.1%).

Financial analyst: Matthias Reith, CIIA, RBI Vienna

GDP: Value added by sector

Change (% yoy, in real terms)	2016	2017e	2018f	2019f
Agriculture & forestry	2.7	-2.0	1.0	0.0
Prod. of goods/mining	1.3	6.8	5.0	2.7
Energy/water supply	1.2	13.0	6.0	1.0
Construction	0.6	4.4	2.6	2.4
Wholesale and retail trade	1.4	3.0	2.7	2.4
Transportation	0.2	2.9	1.9	1.4
Accom. & restaurant trade	2.5	2.1	3.0	2.0
Information and communication	1.2	1.9	1.3	0.8
Credit and insurance	0.3	1.2	0.8	0.5
Property & business services	1.6	1.5	2.6	2.2
Other economic services	1.9	3.1	2.5	1.5
Public sector	1.6	0.8	1.0	1.0
Healthcare, social services	1.7	1.7	1.5	1.3
Other services	-0.7	0.8	1.5	1.2
Gross domestic product	1.5	3.2	2.6	1.6

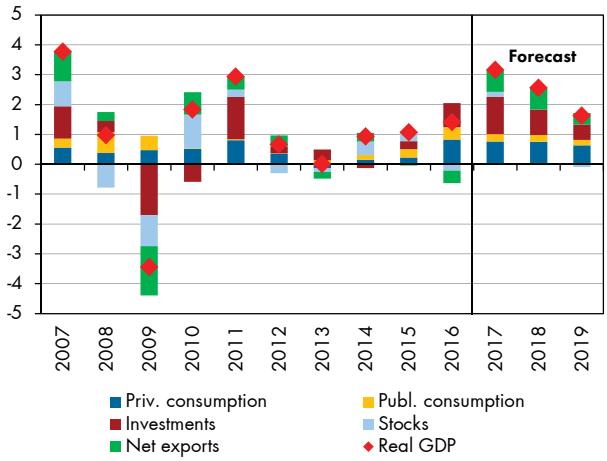
Source: Statistics Austria, RBI/Raiffeisen RESEARCH

GDP: Expenditure composition

Change (% yoy, in real terms)	2016	2017e	2018f	2019f
Private consumption	1.5	1.5	1.5	1.3
Public consumption	2.1	1.2	1.2	0.9
Gross fixed capital formation	3.7	5.4	3.6	2.2
Equipment	8.6	7.9	3.5	2.0
Construction	1.1	3.3	2.6	2.1
Exports	1.9	6.0	4.5	3.1
Imports	3.1	5.0	3.5	2.7
Gross domestic product	1.5	3.2	2.6	1.6

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

Contributions* to real GDP growth (yoy)

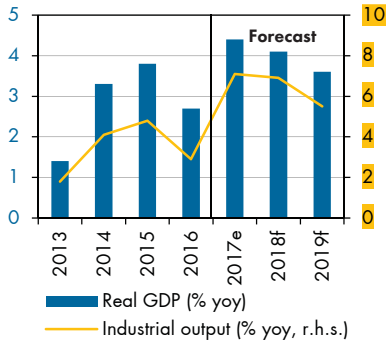


** in percentage points*
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Impressive economic growth in Q3

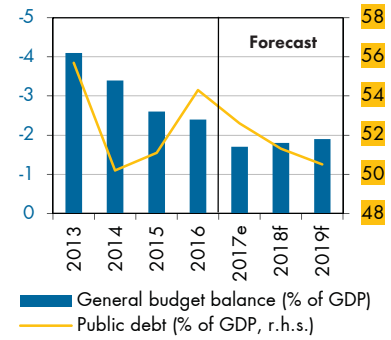
- **Investment demand still below expectations; limited impact of pension reform on employment**
- **Fiscal stability strengthened by low deficit**
- **Mounting speculations about rate hikes to support PLN in first half of 2018**
- **Yields bound to rise as tightening cycle approaches**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: National sources, RBI/Raiffeisen RESEARCH

Economic outlook

Economic growth in Q3 satisfied almost everyone. Optimists emphasised the GDP acceleration to 4.9% yoy, well above the market average, and the 0.1pp upwards revision of the data for H1. Robust growth resulted mainly from private consumption which grew 4.8% yoy, and net exports that contributed 1.1pp to the overall growth. Given the strong short-term macroeconomic indicators for October and November, it is justified to **expect robust growth of around 4.5% yoy in Q4.** Meanwhile, those doubting the strength of the Polish economy focused on the low investment activity as gross fixed capital investment increased by a mere 3.3% yoy, even though public investments clearly accelerated, as seen in the construction output figures. Private businesses, however, remain cautious with new outlays. Surveys among businesses show that the key factor limiting activity is the labour market, as a growing number of firms face problems with finding employees, especially highly qualified ones. Meanwhile, the share of companies signalling uncertainty about future demand or the unclear legal environment is declining.

So we believe that the **low investment activity mainly stems from the labour market** as the lack of qualified workers can lower capital productivity. Besides, the share of companies indicating a lack of appropriate equipment as the barrier to growth has stabilised at a low level, close to 10% for manufacturers, suggesting that firms may simply need human capital instead of physical capital. Based on this information we decided to lower our investment forecast, even though the increased inflow of EU-related projects is still expected to boost public investment. However, we are now much more optimistic on private consumption. Both the October data on corporate employment and November's PMI index did not show any decline in jobs, despite the lower retirement age coming into force in October. Of course it is too early to make a full assessment of the reform and its consequences, but it seems that in the short and medium term the effects will

Key economic figures and forecasts

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	395	411	430	424	464	507	534
Real GDP (% yoy)	1.4	3.3	3.8	2.7	4.4	4.1	3.6
Industrial output (% yoy)	1.8	4.1	4.8	2.9	7.1	6.9	5.5
Unemployment rate (avg, %)	13.5	12.3	10.5	8.9	7.3	5.8	4.8
Nominal industrial wages (% yoy)	2.9	3.7	3.5	4.1	5.7	7.3	7.1
Producer prices (avg, % yoy)	-1.3	-1.5	-2.2	-0.1	3.3	3.4	2.7
Consumer prices (avg, % yoy)	0.9	0.0	-0.9	-0.6	2.0	2.3	2.6
Consumer prices (eop, % yoy)	0.7	-1.0	-0.5	0.8	2.2	2.4	2.7
General budget balance (% of GDP)	-4.1	-3.4	-2.6	-2.4	-1.7	-1.8	-1.9
Public debt (% of GDP)	55.7	50.2	51.1	54.3	52.6	51.3	50.5
Current account balance (% of GDP)	-1.3	-2.1	-0.6	-0.3	-0.3	-1.0	-1.4
Official FX reserves (EUR bn)	77	83	87	108	97	106	110
Gross foreign debt (% of GDP)	70.6	71.4	70.2	74.5	72.7	71.1	65.6
EUR/PLN (avg)	4.20	4.19	4.18	4.36	4.26	4.16	4.20
USD/PLN (avg)	3.16	3.16	3.77	3.95	3.74	3.47	3.28

Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

concentrate on public finance and wages as firms will have to increase salaries to keep their most valuable workers and attract previously inactive labour. Given such a scenario, the **wage fund in the economy may grow faster and provide a solid base for consumption growth**.

The total cost of the pension reform to public finance could approach approximately PLN 10 bn in 2018, which, however, does not threaten safe budget levels. With strong economic growth in Europe the Ministry of Finance can still profit from cyclical improvements in tax collection in 2018. The government is also still struggling hard to seal the tax system. It is estimated that the introduction of split payments will bring PLN 0.4 bn in additional VAT income in 2018, increasing in the following years to PLN 9 bn by 2023.

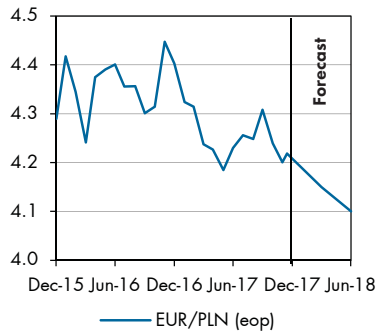
It seems that domestic **CPI has returned permanently above 2% yoy, and it may even breach 2.5% in 2018** driven not only by commodities but also by accelerating core inflation. The upwards trend in domestic CPI in 2018 may, however, be only gradual as the transmission from labour market into CPI remains distorted. Furthermore, the increase in the output gap may be slower than we previously assumed as potential GDP growth seems to be less affected by the lower retirement age.

Financial market outlook

With inflation staying within the official range of 2.5% +/- 1pp the situation of the Polish MPC has become quite inconvenient. Economic growth is widely expected to stay strong, and the **real interest rate fell deep into negative territory towards the end of 2017**, which is unacceptable for some MPC members. The majority of the Council, however, is unlikely to change its dovish rhetoric until the CPI remains permanently above 2%, which, in our opinion, is possible in early Q2 2018. With that in mind we stick to our forecast of a first interest rate hike in Poland in Q3 2018. As in the previous quarter, the main risk for Poland is politics due to the still unresolved conflict between Poland and the EU regarding the ongoing reform of the Polish judicial system. While the EU launched an infringement procedure for breach of the rule of law, the risk of the most extreme sanctions remains very low since there is no unanimous support among Member States. Meanwhile, it remains to be seen whether relations between the EU and Poland improve under the new Prime Minister, former banker and previous Minister of Development and Finance, M. Morawiecki, who replaced B. Szydło in December. **The EUR/PLN managed to reach 4.20 vs the euro** supported by the favourable market and economic environment in Q4. Although the MPC will stick to its neutral stance overall, recurring rate-hike speculations could contribute to some zloty strengthening. We could therefore see the EUR/PLN edge closer to 4.10-4.15 in mid-2018. As investors price in rate increases by the MPC later in H1 2018 this should also drive Polish yields higher, albeit only moderately.

Financial analysts: Dorota Strauch, CFA; Pawel Radwanski, Raiffeisen Polbank, Warsaw

Exchange rate development



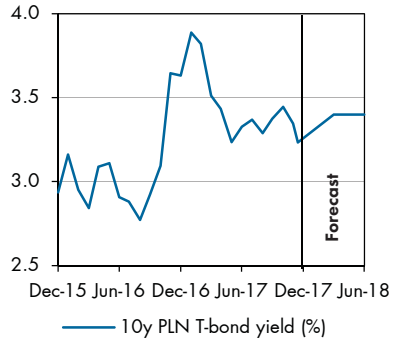
EUR/PLN: 5y high 4.5, 5y low 3.99
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
EUR/PLN	4.22	4.15	4.10	4.15	4.20
Cons.		*4.20*	*4.20*	*4.17*	*4.15*
USD/PLN	3.58	3.61	3.42	3.40	3.39
Cons.		*3.60*	*3.54*	*3.48*	*3.46*

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

PLN yield development (%)



10y PLN T-bond yield: 5y high 4.86, 5y low 2
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
Key rate	1.50	1.50	1.50	1.75	2.00
Consensus		*1.50*	*1.55*	*1.60*	*1.75*
3 month[2]	1.72	1.73	1.90	2.15	2.40
Consensus		*1.73*	*1.74*	*1.81*	*1.90*

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

Yield forecasts (%)

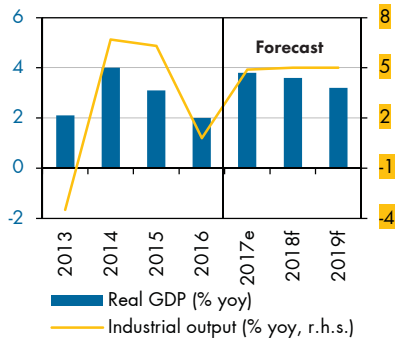
	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
2y T-bond[2]	1.66	2.1	2.2	2.3	2.4
Consensus		*1.9*	*2.1*	*2.3*	*2.4*
10y T-bond[2]	3.23	3.4	3.4	3.5	3.6
Consensus		*3.6*	*3.7*	*3.9*	*4.1*

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

Pro-cyclical policy helps growth peak

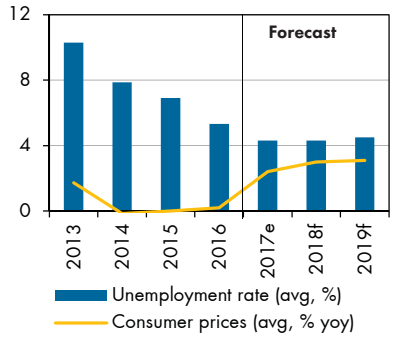
- **Close to 4% GDP growth in 2018-2019 driven by domestic demand**
- **External/fiscal balances deteriorate but no cause for concern yet**
- **Inflation expected to reach 3% target by mid-2018**
- **MNB keeps rates depressed – HUF markets likely to weaken mildly**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Inflation and unemployment



Source: National sources, RBI/Raiffeisen RESEARCH

Economic outlook

The Hungarian **economy is growing at nearly full speed in 2017, close to 4%.** The growth is mainly driven by domestic demand, something which by and large was missing from the last decade. Rising private household consumption is not a new phenomenon as it has gradually been accelerating over past years, driven by strong real income growth. Nevertheless, its pace does not exceed that of GDP growth. 2017 brought a **breakthrough in gross fixed capital formation:** after the meagre performance in previous years there is now an investment boom with a 23% yoy rise in the first three quarters of 2017. There are various reasons for such a turn: EU funds utilisation has picked up; government spending is accelerating in light of the forthcoming elections; companies underinvested in previous years, now their investment demand is backed by accessible loans. Another reason can be found in the general scarcity of labour, as investing into modern technologies is often a way of finding a solution at the micro level. Going forward, if this strong capex activity becomes widespread and persists for several years, the **technological advancement may lift the growth potential of the whole economy**. Strong domestic demand with its import content is also impairing the external balances. Nevertheless, this is very mild for the time being: the trade surplus decreased from EUR 8.4 bn to EUR 7 bn in the first ten months of the year (2016 vs 2017), while the service balance remained more or less unchanged. In 2018 and 2019 export capacity increases (especially, but not exclusively, in the car industry) may well slow down the rate of deterioration. Fiscal policy is pro-cyclical and fuels growth through wage policy and by driving public-sector investments. Since **2018 and 2019 are election years** (Q2 2018 parliamentary elections; Q3 2019 municipal elections) we expect the loose fiscal stance to stay – however, the 3% deficit threshold is unlikely to be breached. Strong wage growth (+13% in 2017; 9% expected for 2018) has so far had little impact on

Key economic figures and forecasts

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	101.5	105.0	109.7	112.4	120.7	125.8	132.5
Real GDP (% yoy)	2.1	4.0	3.1	2.0	3.8	3.6	3.2
Industrial output (% yoy)	-3.5	6.7	6.3	0.8	4.9	5.0	5.0
Unemployment rate (avg, %)	10.3	7.9	6.9	5.3	4.3	4.3	4.5
Nominal industrial wages (% yoy)	4.4	4.0	5.3	7.5	12.0	8.8	5.8
Producer prices (avg, % yoy)	0.7	-0.4	-0.7	-1.7	2.9	3.4	3.2
Consumer prices (avg, % yoy)	1.7	-0.2	0.0	0.2	2.4	3.0	3.1
Consumer prices (eop, % yoy)	0.4	-0.9	0.9	1.1	2.6	3.0	3.2
General budget balance (% of GDP)	-2.3	-2.5	-2.0	-2.0	-2.5	-3.0	-3.0
Public debt (% of GDP)	76.8	76.2	75.2	73.9	72.9	71.9	71.1
Current account balance (% of GDP)	4.1	3.9	3.4	5.4	3.2	2.9	2.7
Official FX reserves (EUR bn)	33.8	34.7	30.5	24.5	23.6	21.2	18.8
Gross foreign debt (% of GDP)	118.1	114.0	106.2	98.3	88.2	83.1	77.3
EUR/HUF (avg)	296.8	308.7	309.9	311.5	309.5	316.8	320.0
USD/HUF (avg)	223.6	232.8	279.4	281.6	271.5	264.0	250.0

Source: National sources, RBI/Raiffeisen RESEARCH

inflation developments. We expect this will change, and **by mid-2018 we will see inflation at the 3% target.** However, the most recent inflation data (H2 2017) signals some downside risks to our inflation forecast. **Economic growth** is being helped by a pro-cyclical policy mix, and is expected to stay close to **4% in 2018** too.

Financial analyst: Zoltán Török, Raiffeisen Bank Zrt., Budapest

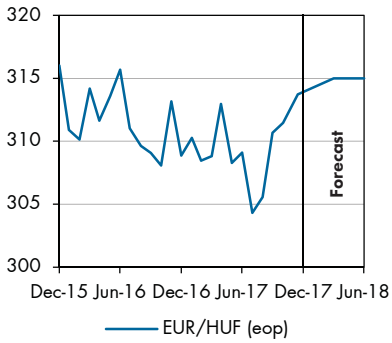
Financial market outlook

Despite the fast wage growth and the strong economic activity, the **National Bank of Hungary (MNB) is continuing with its expansionary policy.** Now that the short end of the curve has been successfully reduced to around zero, the MNB has just taken targeted measures to drive longer maturities down too. The Monetary Council announced in November that it would introduce 5- and 10y IRS tenders, and start buying mortgage notes on the primary and secondary market as well from January 2018 to flatten the curve and encourage lending at cheaper fixed rates, which are currently sold at much higher premiums than in other peer countries. Furthermore, the MNB also wants to reduce macro-prudential risks stemming from the future normalisation of the BUBOR rates by increasing the ratio of the fixed-rate retail housing loans mentioned. The size of the program is significant (HUF 1,000-1,500 bn IRS scheme and up to HUF 500 bn mortgage bond scheme, so called QE), and that is expected to drive the longer end down further. Since the announcement, **HUF swap rates and 5-15y HGB yields have fallen to new lows**. Looking ahead, yields and rates could somewhat fall further in the coming months, as the actual measures will start from 2018, however, we do not think there is still room for another decline the likes of which we experienced in the last quarter. We will need to see the new measures in action, but the strong ambitions of the MNB and the very first market reactions make us believe that they will be effective not only in the short-term, but even in the medium-term, and will allow at least 5-15y HGB yields to increase only moderately. **We uphold our call for the first interest rate hike to come only from end-2019**, and for BUBOR rates to rise from end-2018.

As far as the forint is concerned, these low levels on the HGB market triggered profit-taking (non-resident share declined further), while HUF sellers returned to the market again, pushing the EUR/HUF above the upper end of the range at 315. **The HUF is now an underperformer**, and since monetary policy divergences among MNB and hawkish peers will surely drive the market in the coming quarters, this underperformance (meaning EUR/HUF around 315-320 in 2018-2019) will remain in place.

Financial analyst: Gergely Pálffy, Raiffeisen Bank Zrt., Budapest

Exchange rate development



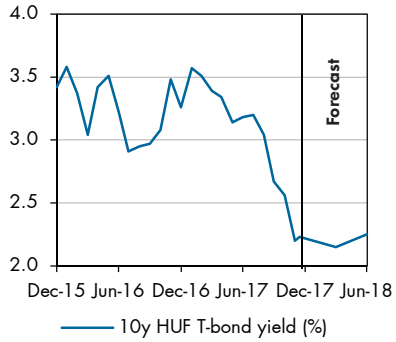
EUR/HUF: 5y high 321.02, 5y low 285.48
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
EUR/HUF	313.71	315	315	320	320
Cons.		*312*	*312*	*310*	*310*
USD/HUF	266.41	274	263	262	258
Cons.		*263*	*256*	*254*	*251*

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

HUF yield development (%)



10y HUF T-bond yield: 5y high 6.87, 5y low 2.11
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
Key rate	0.90	0.90	0.90	0.90	0.90
Consensus		*0.90*	*0.90*	*0.95*	*1.05*
3 month[2]	0.03	0.05	0.05	0.05	0.20
Consensus		*0.11*	*0.20*	*0.35*	*0.47*

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

Yield forecasts (%)

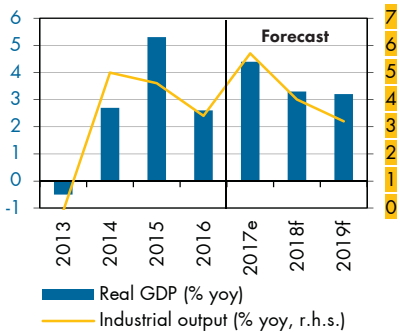
	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
3y T-bond[2]	0.67	0.6	0.7	0.8	1.0
Consensus		*n.v.*	*n.v.*	*n.v.*	*n.v.*
10y T-bond[2]	2.23	2.2	2.3	2.4	2.4
Consensus		*2.40*	*2.31*	*2.53*	*2.70*

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

Economy at a cyclical peak

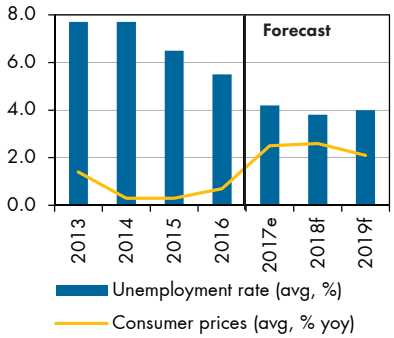
- **GDP growth healthy and sustainable, but limited by slow productivity growth**
- **Inflation to gradually descend to CNB's 2% target in 2018**
- **Further normalisation of CNB monetary policy**
- **Gradual upwards shift expected amidst bear flattening of yield curve**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Inflation and unemployment



Source: National sources, RBI/Raiffeisen RESEARCH

Economic outlook

The Czech Republic is experiencing a year of an ever-accelerating economic recovery, with **GDP growth reaching 0.5% qoq and 5.0% yoy in Q3 2017.** While the fast pace of economic growth in the previous two years was largely driven by extraordinary investment growth as a result of increased EU funding, this year's GDP growth draws from a wider and more sustainable source. All demand-side components contributed to GDP fairly equally, most notably investment expenditure, private consumption and the positive trade balance. There is strong evidence that the recovery of investment activity will continue. **Industrial production growth has been very strong this year**, and this will hold true for the first half of 2018. On the other hand, export growth has probably peaked, while imports have been catching up due to increased prices of raw materials. Moreover, the CZK appreciation will further limit export growth and so the currently strong contribution from positive foreign trade is likely to be reduced. Solid results in Q2 and Q3 point to average GDP growth of 4.4% in 2017, according to our estimate. But **in Q1 2018 we anticipate a moderate slowdown.** Given the fast pace of growth and the fact that the average economic boom in the Czech Republic lasts about five years, we can assume the economy has peaked in its cycle and will start to descend at the beginning of 2018. Economic booms are linked with higher inflation, and the Czech economy is by no means an exception. **Inflation has been high above the 2% target for the most part of this year.** For next year, however, we predict inflation will slowly and steadily decrease towards the target. The main story of this year is the record tight labour market with **unemployment falling to 3.5%,** the lowest it has been since 1996. Firms are becoming desperate to find workers, which activates long-term labour reserves. But the primary barrier preventing firms from further expansion is the severe lack of qualified workers. Employees are benefiting from this situation with average real wage growth estimated to rise above 6% throughout 2017 and in the beginning of 2018. But real wage growth is now

Key economic figures and forecasts

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	157.7	156.7	168.4	176.6	193.5	214.8	228.1
Real GDP (% yoy)	-0.5	2.7	5.3	2.6	4.4	3.3	3.2
Industrial output (% yoy)	-0.1	5.0	4.6	3.4	5.7	4.0	3.2
Unemployment rate (avg, %)	7.7	7.7	6.5	5.5	4.2	3.8	4.0
Nominal industrial wages (% yoy)	1.0	3.3	2.6	3.8	7.5	8.2	6.6
Producer prices (avg, % yoy)	0.8	-0.8	-3.2	-3.3	1.9	3.0	2.8
Consumer prices (avg, % yoy)	1.4	0.3	0.3	0.7	2.5	2.6	2.1
Consumer prices (eop, % yoy)	1.4	0.1	0.0	2.0	2.7	2.1	2.1
General budget balance (% of GDP)	-1.3	-1.9	-0.6	0.6	0.0	-0.7	-0.4
Public debt (% of GDP)	44.9	42.2	40.3	37.9	34.3	33.1	31.8
Current account balance (% of GDP)	-0.5	0.2	0.2	1.1	1.1	0.7	0.4
Official FX reserves (EUR bn)	40.8	45.0	59.4	81.3	129.4	125.4	119.9
Gross foreign debt (% of GDP)	66.7	70.1	69.5	73.9	89.6	86.6	83.5
EUR/CZK (avg)	26.0	27.5	27.3	27.0	26.4	25.2	24.9
USD/CZK (avg)	19.6	20.8	24.6	24.4	23.1	21.0	19.5

Source: National sources, RBI/Raiffeisen RESEARCH

more than twice as high as productivity growth. The only solution to the shortage of workers has to come through intensive investment in the productivity of labour.

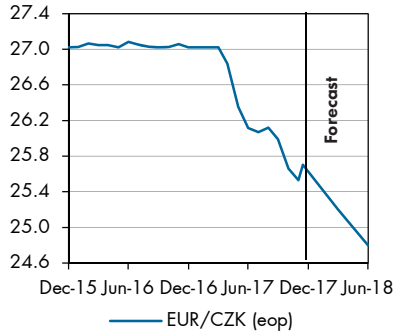
Financial analysts: Milan Frydrych, Raiffeisenbank a.s., Prague

Financial market outlook

In Q4 2017 the koruna strengthened even more quickly in anticipation of a faster normalisation of CNB monetary policy and the shrinking gap between spot rates and the long-term equilibrium FX rate. The central bank's first hike originally seemed to be an isolated event, but the **current economic development calls for further tightening**. This has made the koruna an attractive investment in CEE, and there has been no massive outflow of speculative capital, in fact, the opposite has happened. Until mid-2018 we expect further strengthening towards EUR/CZK 24.80, but thereafter, with the ECB monetary policy starting to tighten and the performance of the Czech economy weakening, there could be a correction in the koruna in H2 2018. So **by the end of 2018 we expect the koruna will weaken to EUR/CZK 25.0**. Since the start of monetary policy normalisation the money market has experienced a significant increase in interest rates, but in recent weeks, money market rates have declined slightly due to a combination of events. At the end of the year, money market rates regularly decrease as a result of commercial banks having to comply with regulatory contributions to the local resolution fund. This creates an excessive supply of funds on the market and money market rates fall. Moreover, we expect a natural mitigation of the exaggerated market expectations of the continued increase in CNB interest rates, which will return money market rates back to lower levels. These effects will disappear at the beginning of 2018 and money market rates will rise again. **Over the coming quarters we expect a gradual upwards shift of the entire yield curve.** The spread between Czech and euro area interest rates will continue to rise until Q3 2018, when we expect the ECB's monetary policy will accomodate. Given the good performance of the economy, the tight labour market and high inflation, we expect to see the next three CNB interest-rate hikes in the first three quarters of 2018. The Ministry of Finance has mainly focused on issuing Treasury bills and shorter-dated bonds due to the negative yields on these securities amidst strong demand from foreign investors. Next year the government's budget plans a deficit of CZK 50 bn. This means the government's strong issuance policy is set to continue. Due to the expected bear flattening of the CZGB curve on account of ongoing rate hikes and increasing core market pressure, the Finance Ministry will likely increase the issuance of longer-term CZK government bonds. Nevertheless, the CZGB curve is likely to shift upwards overall in the course of next year, while any temporary CZK weakness could prompt investors to add exposure / enter the market, as long as the long-term CZK appreciation story remains intact. **The major risk is a mass exit of non-resident investors** who have kept their share in total CZK bonds outstanding since CZKexit fairly stable (more than 45% as of end-October).

Financial analysts: František Táborský, Raiffeisenbank a.s., Prague

Exchange rate development



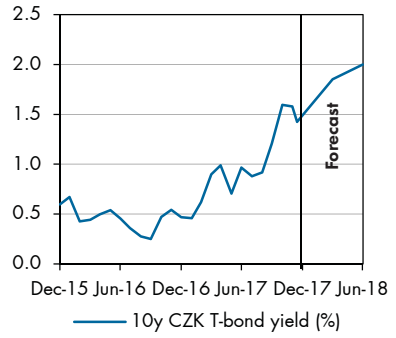
EUR/CZK: 5y high 28.35, 5y low 25.07
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
EUR/CZK	25.71	25.20	24.80	25.30	25.00
Cons.		*25.35*	*25.20*	*25.00*	*25.00*
USD/CZK	21.83	21.91	20.67	20.74	20.16
Cons.		*21.50*	*20.96*	*20.40*	*20.25*

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

CZK yield development (%)



10y CZK T-bond yield: 5y high 2.69, 5y low 0.24
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
Key rate	0.50	0.75	1.00	1.25	1.25
Consensus		*0.75*	*0.95*	*1.10*	*1.20*
3 month[2]	0.76	1.10	1.25	1.45	1.60
Consensus		*0.98*	*1.17*	*1.30*	*1.44*

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

Yield forecasts (%)

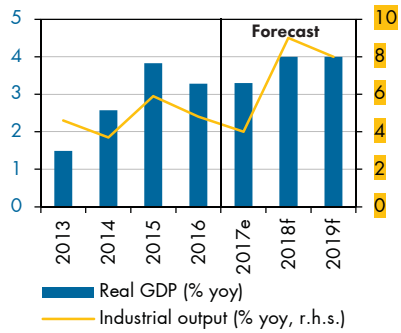
	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
2y T-bond	0.23	0.5	0.8	1.2	1.2
Consensus		*0.7*	*0.9*	*1.0*	*1.1*
10y T-bond	1.43	1.9	2.0	2.2	2.2
Consensus		*1.9*	*2.0*	*2.1*	*2.2*

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

Slovakia – Kick-off for investments?

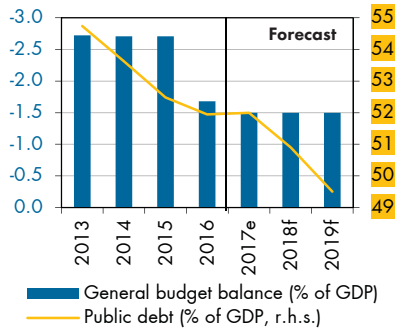
- **Households and investments lift economic growth**
- **Slovaks abroad return home**
- **GDP growth to test top CE ranking in 2018**
- **Deficit consolidation below potential**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: National sources, RBI/Raiffeisen RESEARCH

Economic outlook

In the third **quarter of 2017, private household consumption and investment growth were the two major factors** behind Slovak economic growth according to the Statistical Office of Slovakia. These two components helped the economy grow by 3.4% yoy after 3.7% yoy in Q2 2017. Private consumption posted its fastest growth (4% yoy) since 2008. Good sentiment on the labour market and growing wages materialised in increased household spending, mainly on services. The most positive piece of news was a rebound in capital formation, which had been on a downwards trend since Q2 2016. In Q3 2017 capital formation grew by 10.4% yoy, compared with a decrease of 5.4% yoy in Q2 2017. The revival of investments (10.4% yoy) was visible especially with machinery and vehicles. Government consumption (-1.4% yoy) and government investments (-11.7% yoy), however, dragged economic growth down. **In 2017 headline GDP growth is fully in line with our expectations and should reach 3.3% yoy. In the course of the coming quarters GDP growth should be more balanced,** and not reliant solely on domestic demand. Bratislava's automotive company is to start producing new models and even a brand new car, the Audi Q8. In the second half of next year, Jaguar Land Rover is to launch its production, which should accelerate GDP growth even more. Together with better-than-expected improvements in the external environment (mainly the euro area) we reckon the Slovak economy will grow by 4% yoy with an upside risk of a higher result. If our expectations materialise, the Slovak economy will be vying for the position of the growing fastest economy in the region. Besides the strong inflow of foreigners into the Slovak labour market, we have noticed a trend of Slovak citizens returning to Slovakia. A strong inflow of people was recently recorded from Great Britain as the Brexit talks make people uncertain about their future. Employment continues growing strongly, by 1.6% yoy. Unemployment, however, dropped by only 0.1pp to 8.0% due to the seasonal increase of graduates entering the job market. Wage growth remains strong, accelerating from 4.8% yoy in Q2 2017 to 5.2% yoy

Key economic figures and forecasts*

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	74.2	75.9	78.7	81.0	84.5	89.5	95.0
Real GDP (% yoy)	1.5	2.6	3.8	3.3	3.3	4.0	4.0
Industrial output (% yoy)	4.6	3.7	5.9	4.8	4.0	9.0	8.0
Unemployment rate (avg, %)	14.2	13.2	11.5	9.7	7.9	7.0	6.2
Nominal industrial wages (% yoy)	3.6	5.4	3.2	3.4	4.8	4.5	4.5
Producer prices (avg, % yoy)	-0.1	-3.5	-4.2	-4.3	0.0	2.0	2.0
Consumer prices (avg, % yoy)	1.4	-0.1	-0.3	-0.5	1.3	2.1	2.0
Consumer prices (eop, % yoy)	0.4	-0.1	-0.5	0.2	1.4	1.8	2.1
General budget balance (% of GDP)	-2.7	-2.7	-2.7	-1.7	-1.5	-1.5	-1.5
Public debt (% of GDP)	54.7	53.6	52.5	51.9	52.0	50.9	49.5
Current account balance (% of GDP)	1.8	1.2	0.2	-0.6	-0.6	0.1	1.2
Gross foreign debt (% of GDP)	81.5	89.2	85.4	88.8	96.2	93.8	91.5

** euro area entry on 1 January 2009*
Source: National sources, RBI/Raiffeisen RESEARCH

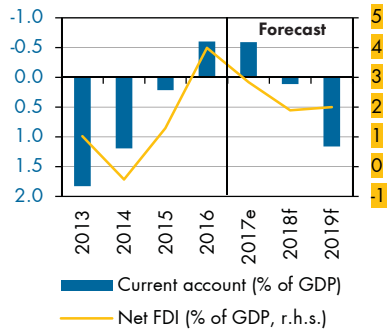
in Q3 2017. Both wages in the private and the public sector made significant contributions. Average wage growth should be around 4.5% yoy in 2017. We expect these **dynamics in both the economy and the labour market to continue in the following quarters.**

The government coalition is stable and it seems they will be able to stay in power until the next regular elections in 2020. Regional elections took place in November 2017. The main point of interest was the performance of the far-right party ĽSNS, which recorded their first strong result four years ago in the previous regional elections. The far-right party lost the region Banská Bystrica by a big margin, and did not succeed elsewhere either. Moreover, the party was able to get only two members into regional parliaments across the whole country. The second interesting fact was that the ruling party SMER-SD lost four out of six regional heads, and representatives of the opposition's parties were successful. This confirms the long-standing declining popularity of the coalition parties. It seems the government has given up the possibility of loosening the "debt brake" – a constitutional law that caps government debt at 60% of GDP. We see this as a positive sign because we believe the current debt brake is satisfactory.

The government deficit stood at 2.2% of GDP in 2016 despite a target of 1.9% of GDP. As for 2017, the government expects the deficit to fall to 1.6% of GDP, a feasible number. In the next couple of years the deficit should drop further to zero, though we have our doubts given the government's inability to achieve targets in the last couple of years. Therefore we remain cautious and forecast a deficit of 1.5% of GDP in the coming years. Even in that case (more pessimistic scenario on deficit development), public debt should fall to around 50.9% of GDP in 2018. From an international perspective this level of debt is quite pleasing, but the debt ratio of the Czech Republic is expected to be 35.2% of GDP in 2017. The Slovak government should use these good times to decrease the deficit in line with its own plans.

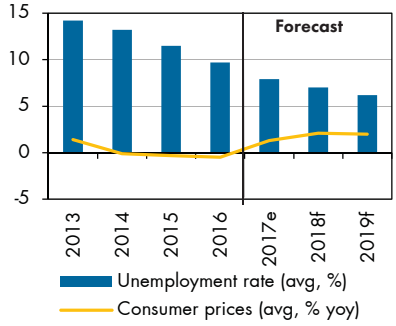
Financial analysts: Boris Fojtík, Juraj Valachy, Tatra banka, a.s. Bratislava

Current account and FDI inflows



Source: National sources, RBI/Raiffeisen RESEARCH

Inflation and unemployment



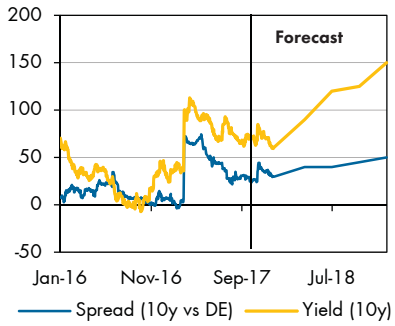
Source: National sources, RBI/Raiffeisen RESEARCH

Financial market outlook

With weak supply on the primary market in Q2 2017, the risk premium on Slovakian government bonds (10Y vs DE) narrowed to 35bp. In light of the robust fundamental data (economy and financing structure), this seems appropriate in comparison to the peer group, but we see it as the lower edge of what we deem to be a fair level. In 2018, the market operations of the ECB (net bond purchases and reinvestment) will continue to significantly influence the risk premium on Slovakian government bonds. The halving of the ECB's purchase programme starting from January will probably have little impact on the monthly volume of purchases of Slovakian government bonds. After all, the target value has been missed by around 50% for more than a year now. At the same time, based on the deficit forecast, no significant expansion in the supply of government bonds is anticipated in 2018. In this environment, over the short run (1–4 months) we see little leeway for a substantial increase in the risk premium and thus recommend holding Slovakian government bonds (10Y) versus the German benchmark. Over the long run, we believe that Slovakian government bonds will remain in the high yield core segment of the EUR government bond market.

Financial analyst: Patrick Krizan, RBI Vienna

Yield and spread*

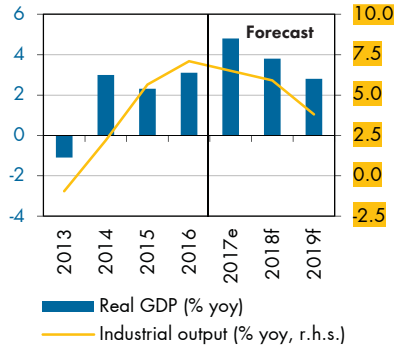


**in basis points*
Spread: 5y high: 424; 5y low: -4
Yield (10y): 5y high: 548; 5y low: -7
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Economy in best shape since ten years

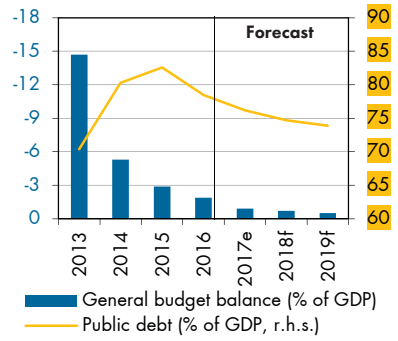
- **Dynamic economic performance in the first three quarters of 2017, driven by net exports and domestic demand**
- **However, closed output gap and GDP growth above potential point to mounting overutilisation of economic capacities**
- **Unemployment continues to fall, but will probably not reach an all-time low during the current business cycle**
- **Slovenian government bonds advance to "semi-core" range**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: National sources, RBI/Raiffeisen RESEARCH

The **Slovenian economy remains very dynamic**. During the first three quarters of 2017, real GDP expanded at an average rate of 1.2% qoq, driven by domestic demand and net exports. Prospects for the coming months also look very good. Economic confidence is ranging at the highest levels recorded since July 2007. The **excellent economic performance in the first three quarters of 2017 confirms our assumption that GDP growth will reach around 5% yoy** for 2017 as a whole, as our current projection of 4.8% yoy has some mild upside risks. Consequently, Slovenia will not only register the strongest GDP growth since 2007, it will also boast the highest growth rate of any of the CE countries. Due to the positive economic performance in 2017 and the good outlook, we have however raised our **growth expectations for 2018 to 3.8% yoy from 3.5% yoy** (2019: 2.8% yoy from 2.6% yoy). In light of the closed output gap and a relatively low potential growth rate, despite the outlook for a moderation of GDP growth rates, there will probably be a **significant overutilisation of production capacities** in the Slovenian economy, which will be reflected in mounting wage pressure. The good economic conditions also result in steady declines in the rate of unemployment. In contrast to other CE countries, unemployment in Slovenia has only fallen to a cyclical low, and it does not appear that the all-time low will be reached in the current economic cycle.

The risk premium on **Slovenian government bonds** (10y vs Germany) continued to narrow in Q4 2017 and is now at 40bp. Consequently, it remained strongly decoupled from the levels seen in the southern peripheral countries (Italy, Spain) and has reached **the "semi-core" range**, which also includes Ireland and Slovakia. At the current level, we see very little fundamental potential on the downside in the next one to four months. At the same time, however, upside risks remain limited thanks to the bond purchases and reinvestments by the ECB. Accordingly, we expect to see the Slovenian risk premium (vs DE) moving sideways (hold recommendation vs DE). Thanks to the improvement in fundamental data and a positive rating trend, Slovenian government bonds should remain in the "semi-core" segment.

Financial analysts: Matthias Reith, CIIA; Patrick Krizan, RBI Vienna

Key economic figures and forecasts*

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	36.2	37.6	38.8	40.4	43.1	45.4	47.5
Real GDP (% yoy)	-1.1	3.0	2.3	3.1	4.8	3.8	2.8
Industrial output (% yoy)	-0.9	2.2	5.6	7.1	6.5	5.9	3.8
Unemployment rate (avg, %)	10.1	9.7	9.0	8.0	6.6	5.9	5.6
Nominal industrial wages (% yoy)	2.8	3.3	2.1	2.1	2.7	3.4	3.8
Producer prices (avg, % yoy)	0.3	-1.1	-0.5	-1.4	1.2	1.5	1.8
Consumer prices (avg, % yoy)	1.9	0.4	-0.8	-0.2	1.5	1.8	2.3
Consumer prices (eop, % yoy)	0.9	-0.1	-0.6	0.6	1.3	2.2	2.4
General budget balance (% of GDP)	-14.7	-5.3	-2.9	-1.9	-0.9	-0.7	-0.5
Public debt (% of GDP)	70.4	80.3	82.6	78.5	76.2	74.7	73.9
Current account balance (% of GDP)	4.4	5.8	4.4	5.2	6.5	6.3	5.5
Gross foreign debt (% of GDP)	114.9	125.7	120.1	110.9	99.2	95.1	90.3

** euro area entry on 1 January 2007*
Source: National sources, RBI/Raiffeisen RESEARCH

Growth in line with general trend

- **GDP growth beyond expectations**
- **Structural reforms inevitable**
- **Banking sector well prepared for new growth cycle**
- **Weak foreign direct investment due to unattractive environment**

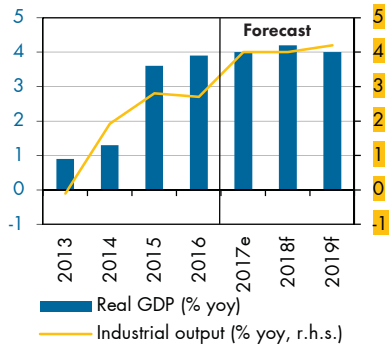
Driven chiefly by household consumption, real GDP grew faster than expected in 2017 (anticipated rate of 4.0%). In turn, gross investment and government consumption also underwent positive developments. Moreover, they are set to accelerate further in Q1 and Q2 2018. The ongoing upward trend in CEE, moving a series of local economic indicators, will further support the Bulgarian economy, which is to accelerate in H1 2018. In line with this trend, the unemployment rate in Q1 and Q2 2018 should remain around 6.0%, while inflation might dip towards 2.0%. Indeed, profiting from the favourable economic conditions (cheap money, relatively low oil prices, and growth trend in EU/CEE) and being politically active in the region around the presidency of the Council of the EU, the **governing coalition is expected to postpone the needed structural reforms during H1 2018** (judiciary, education, health care, pensions and energy sector), replacing them with more budgetary spending for these sectors. So against the backdrop of the ongoing budget surpluses the government has planned a budget deficit of 1% in 2018. Of course, more public spending on the back of the improved absorption of EU funds that is anticipated will boost growth in 2018, though question marks over sustainability still prevail.

In turn, finding its growth path, the **banking sector will also benefit from the economic growth in H1 2018**. Along with expansion in the mortgage and consumer loan segments, business loans are expected to rebound in Q1 and Q2 2018, keeping the sector's capital and liquidity positions strong.

The tense external environment (Syria, Turkey, etc.) along with internal political instability until the middle of the year negatively affected FDI in 2017. Yet the gradual resolution of the conflicts and higher economic growth will have a positive impact on foreign investment, although we do not expect significant FDI growth in H1 2018.

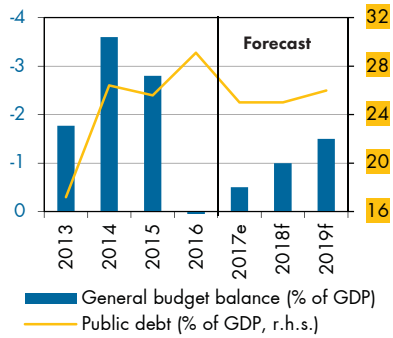
Financial analyst: Emil S. Kalchev, Raiffeisenbank (Bulgaria) EAD, Sofia

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: National sources, RBI/Raiffeisen RESEARCH

Key economic figures and forecasts

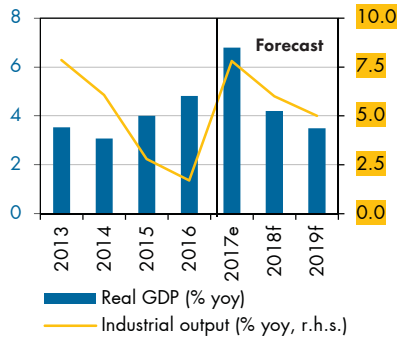
	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	41.9	42.8	45.3	48.1	51.1	54.6	57.1
Real GDP (% yoy)	0.9	1.3	3.6	3.9	4.0	4.2	4.0
Industrial output (% yoy)	-0.1	1.9	2.8	2.7	4.0	4.0	4.2
Unemployment rate (avg, %)	12.9	11.4	9.2	7.6	6.2	5.7	5.5
Nominal industrial wages (% yoy)	3.0	0.9	9.3	8.3	10.5	10.0	9.7
Producer prices (avg, % yoy)	-1.4	-1.2	-1.9	-3.1	1.4	1.9	2.8
Consumer prices (avg, % yoy)	0.9	-1.4	-0.1	-0.8	1.9	2.6	3.1
Consumer prices (eop, % yoy)	-1.6	-0.9	-0.4	0.1	2.5	3.0	3.4
General budget balance (% of GDP)	-1.8	-3.6	-2.8	1.6	-0.5	-1.0	-1.5
Public debt (% of GDP)	17.2	26.4	25.6	29.1	25.0	25.0	26.0
Current account balance (% of GDP)	1.9	0.1	0.4	3.7	6.9	5.5	4.4
Official FX reserves (EUR bn)	14.4	16.6	20.4	23.9	22.3	23.4	23.8
Gross foreign debt (% of GDP)	88.1	92.0	75.3	72.1	63.7	61.3	60.4
EUR/BGN (avg)	1.96	1.96	1.96	1.96	1.96	1.96	1.96
USD/BGN (avg)	1.47	1.47	1.76	1.77	1.72	1.63	1.53

Source: National sources, RBI/Raiffeisen RESEARCH

Overheating concerns increasing

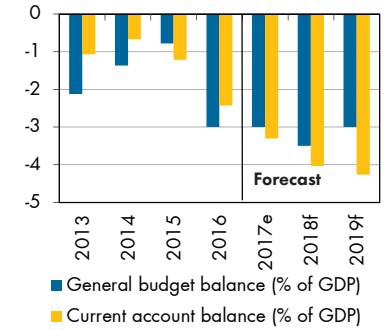
- **Economic growth to remain solid in 2018, growing fiscal deficit a concern**
- **Central bank now outright hawkish as inflation outlook deteriorates sharply**
- **Major change in NBR operational strategy aims to limit volatility of money-market rates**
- **Rates and yields to increase further in 2018 as NBR continues MP tightening**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget and current account balance



Source: National sources, RBI/Raiffeisen RESEARCH

Economic outlook

Economic growth surged in Q3 as real **GDP went up by 2.6% qoq and 8.8% yoy, beating expectations by a large margin.** On the demand side, private consumption was the main driver of GDP growth in Q3 (13.3% yoy, close to the rates recorded in pre-crisis years). Gross fixed investments continued to rebound gradually in Q3, for the third quarter in a row. On the supply side, agriculture spiked in Q3 (33.4% yoy) favoured by the mild weather conditions and by the low base in 2016. Solid increases were also recorded by gross value added in industry and in services. **The very rapid economic growth** registered during Q1-Q3 2017 (7.0%), driven mainly by private consumption, **points towards an overheating economy.** Following the economic growth recorded in Q3, real GDP is likely to have advanced by 6.8% in 2017, outpacing our previous expectations of 5.7%. We expect economic growth to remain solid, but it will decline to a more sustainable level in 2018, i.e. to 4.2%. Private consumption should continue to be the main driver of economic growth as the significant increases in wages and pensions will keep individuals' propensity to spend at elevated levels. Likewise we expect the rebound of investments to remain on track in 2018. The advance in exports of goods and services expected on the back of the improved global demand should continue to be offset by a more rapid increase in imports of goods and services, thus widening the external imbalance. On the supply side, economic growth should be broadly based in 2018 as we look for increases in gross valued added in all sectors of activity.

The deterioration of the fiscal position represents the main macroeconomic risk going forward. The sharp cut in public investments and the one-off payments in special dividends received from state-owned companies were used to prevent the public budget deficit jumping above 3% of GDP in 2017, but such measures are only temporary in nature. While the public budget deficit target for 2018 was set

Key economic figures and forecasts

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	144.3	150.3	160.3	169.6	186.1	198.3	211.0
Real GDP (% yoy)	3.5	3.1	4.0	4.8	6.8	4.2	3.5
Industrial output (% yoy)	7.9	6.1	2.8	1.7	7.8	6.0	5.0
Unemployment rate (avg, %)	7.1	6.8	6.8	5.9	5.0	4.7	4.7
Nominal industrial wages (% yoy)	4.2	7.4	6.6	8.7	12.5	27.0	7.5
Producer prices (avg, % yoy)	2.1	-0.1	-2.2	-1.8	3.7	4.0	3.5
Consumer prices (avg, % yoy)	4.0	1.1	-0.6	-1.5	1.3	4.3	3.3
Consumer prices (eop, % yoy)	1.6	0.8	-0.9	-0.5	3.2	3.5	3.0
General budget balance (% of GDP)	-2.1	-1.4	-0.8	-3.0	-3.0	-3.5	-3.0
Public debt (% of GDP)	37.8	39.4	37.9	37.6	36.7	37.2	37.9
Current account balance (% of GDP)	-1.1	-0.7	-1.2	-2.4	-3.3	-4.0	-4.3
Official FX reserves (EUR bn)	35.4	35.7	35.6	37.9	36.6	37.0	37.8
Gross foreign debt (% of GDP)	68.0	63.0	57.4	54.8	50.8	50.4	51.2
EUR/RON (avg)	4.42	4.44	4.45	4.49	4.57	4.67	4.68
USD/RON (avg)	3.33	3.35	4.01	4.06	4.01	3.89	3.66

Source: National sources, RBI/Raiffeisen RESEARCH

at 3% of GDP, we see a good chance of this being exceeded (our forecast is 3.5% of GDP) unless corrective measures are taken. So the uncertainty related to the Government's policies should remain elevated in the forthcoming period.

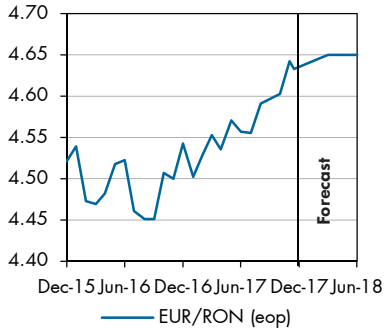
Inflation dynamics came in far above expectations over recent months as the underlying inflationary pressures strengthened more than expected and several large adverse supply-side shocks materialised (increase in administered prices, hike of excise duties on fuels, increase in oil price, leu depreciation). The **annual inflation rate reached 3.2%** in November and it should continue on a sustained upwards trend in the following months, likely peaking close to 5% in Q2 2018. The main drivers for the rapid advance in annual inflation in the coming quarters include a dissipation of the favourable statistical base effect fuelled by tax cuts in January-February 2017, an increase in administered prices and an additional strengthening of underlying inflationary pressures.

Financial market outlook

Unexpectedly the central bank has become outright hawkish following the sharp deterioration of the inflation outlook and the increase in investors' risk aversion towards Romania (due to elevated uncertainty surrounding the Government's policies and an increase in macroeconomic imbalances). After a liquidity shortage emerged on the money market at the beginning of October and **money-market interest rates jumped by more than 100bp** (outpacing the monetary policy rate of 1.75%), the NBR announced a change in strategy at the monetary-policy meeting from November. Going forward, the NBR now aims to reduce the volatility of interest rates, keeping them in the vicinity of the monetary policy rate. To achieve its new objective it is willing to accept larger fluctuations in the leu exchange rate. Given the new macroeconomic conditions and the change in central bank's rhetoric and strategy, we now think that monetary policy tightening will proceed at a faster pace than we previously expected. **We see the central bank increasing the key rate five times in 2018** (instead of the previous three times), from 1.75% to 3.0%. This should keep money-market interest rates and yields of RON government securities on an upwards trend in 2018, even though these jumped in recent months. While the elevated level of interest rates will be beneficial for the leu, we still see room for some leu depreciation in 2018.

Financial analysts: Nicolae Covrig, CFA, Silvia Maria Rosca, Raiffeisen BANK S.A., Bucharest

Exchange rate development



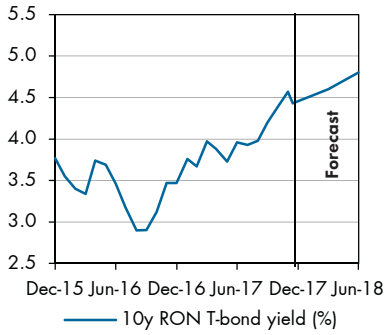
EUR/RON: 5y high 4.65, 5y low 4.3
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
EUR/RON	4.63	4.65	4.65	4.70	4.70
Cons.		*4.64*	*4.64*	*4.65*	*4.65*
USD/RON	3.93	4.04	3.88	3.85	3.79
Cons.		*3.91*	*3.88*	*3.82*	*3.81*

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

RON yield development (%)



10y RON T-bond yield: 5y high 6.9, 5y low 2.66
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
Key rate	1.75	2.25	2.50	2.75	3.00
Consensus		*2.00*	*2.15*	*2.40*	*2.60*
3 month[2]	2.13	2.50	2.75	3.00	3.30
Consensus		*2.11*	*2.31*	*2.48*	*2.73*

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

Yield forecasts (%)

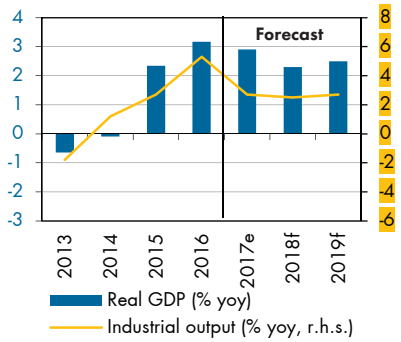
	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
3y T-bond[2]	3.45	3.8	4.0	4.1	4.2
Consensus		*2.1*	*2.2*	*2.2*	*2.4*
10y T-bond[2]	4.43	4.6	4.8	4.9	5.0
Consensus		*4.4*	*4.5*	*4.6*	*4.7*

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

Seems good, but is it enough?

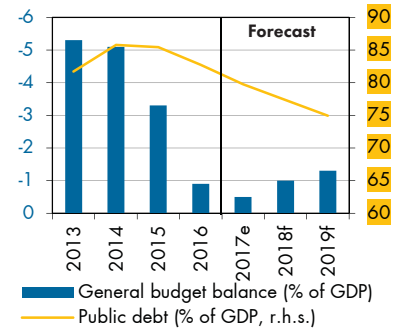
- **Broad-based recovery continues**
- **Long-term challenges remain unchanged**
- **Further (mainly cyclical) improvement in fiscal metrics**
- **Monetary policy – fully committed to EUR/HRK stability**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: National sources, RBI/Raiffeisen RESEARCH

Economic outlook

In line with expectations, 2017 growth has continued at a pace resembling 2016. Through the quarters the recovery has remained broad-based, driven primarily by exports and household consumption. Moreover, both components surpassed expectations, thus neutralising the slowdown in investment. The latter refers primarily to the public sector, particularly investments connected to the utilisation of EU funds.

Still, the overall picture as well as the short-term outlook remains favourable, especially considering the external environment, i.e. the improved external demand and the prolonged period of low interest rates. Besides the base effect, **the projected slowdown in 2018 is primarily connected to the (orderly) restructuring of Agrokor**, which has had a limited impact on the overall economy so far. We remain firm in our forecast that 2018 will be more challenging in this respect. However, the final resolution of the Agrokor situation is still a big factor of uncertainty. Otherwise, 2018 GDP growth could approach 3% yoy for the third year in a row. At any rate, the negative output gap will close by the end of the year.

The rising optimism in the European and regional markets, paired with more positive growth forecasts from Croatia's main trading partners, is fuelling expectations that exports will maintain their healthy growth in the forthcoming quarters. However, as is now customary, the very large import dependency will result in a negative contribution from net exports. As **for the biggest GDP component, household consumption, we expect to see some solid development** especially in H1 2018. Besides tourism and the related positive spill-overs, the lack of labour in certain activities will exert further pressure on wages. Moreover, it seems that the Government has already supported spending by raising the minimum salary and wages in the public sector. Finally, projects supported by EU

Key economic figures and forecasts

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	43.7	43.4	44.5	46.4	48.8	50.8	53.0
Real GDP (% yoy)	-0.6	-0.1	2.3	3.2	2.9	2.3	2.5
Industrial output (% yoy)	-1.8	1.2	2.7	5.3	2.7	2.5	2.7
Unemployment rate (avg, %)	17.4	17.3	16.3	13.1	11.7	11.1	10.2
Nominal industrial wages (% yoy)	1.7	1.5	-4.1	2.0	4.2	3.1	2.3
Producer prices (avg, % yoy)	0.5	-2.7	-3.9	-4.1	2.2	2.8	2.4
Consumer prices (avg, % yoy)	2.2	-0.2	-0.5	-1.1	1.2	1.4	2.0
Consumer prices (eop, % yoy)	0.3	-0.5	-0.6	0.2	2.0	1.3	1.5
General budget balance (% of GDP)	-5.3	-5.1	-3.3	-0.9	-0.5	-1.0	-1.3
Public debt (% of GDP)	81.7	85.8	85.4	82.7	79.8	77.4	74.9
Current account balance (% of GDP)	1.0	2.0	4.7	2.5	3.6	2.2	2.5
Official FX reserves (EUR bn)	12.9	12.7	13.8	13.5	15.1	15.4	15.5
Gross foreign debt (% of GDP)	104.7	107.0	101.9	89.8	82.5	79.7	76.3
EUR/HRK (avg)	7.58	7.63	7.61	7.53	7.46	7.46	7.48
USD/HRK (avg)	5.71	5.76	6.86	6.81	6.54	6.22	5.84

Source: National sources, RBI/Raiffeisen RESEARCH

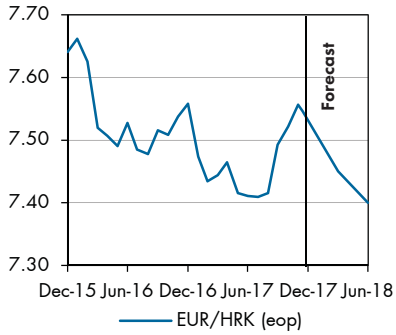
funds that are expected to be utilised better during 2018, as well as private-sector investments (primarily in tourism), will continue to generate investment growth. Such a growth structure very much favours the revenue side of the budget, which relies particularly on indirect taxes, primarily VAT. So with nominal restraint in spending, the headline budget deficit remains at 1% of GDP, implying a solid primary surplus (above 2% of GDP) and a further reduction of public debt. Of course, nothing has changed in the structure of expenditure, which has been the same for many years; this indicates that the reforms much needed for long-term stable, sustainable and higher growth are still pending. And these are exactly the reasons for the very slow recovery in Croatia, which has taken a decade to return to its pre-crisis level (2008) in terms of economic development.

Financial market outlook

Although relatively demanding, 2017 might be deemed quite successful in terms of sovereign refinancing. The government fulfilled its refinancing needs back in November after issuing the Eurobond and the pure local HRK bond. As announced, the Eurobond issuance has been used for the financial restructuring of the Croatian road sector (Croatian Motorways and Motorway Rijeka - Zagreb), which is a very large holder of public debt (EUR 5.2 bn). The financial restructuring of the remaining debt portfolio will take place during Q1 2018 on a bilateral level with financial institutions (banks). We can undoubtedly say that the maturity and interest rate cost of public debt has improved already. We expect **the government might tap the international and local market no later than Q2 2018**. Besides the favourable timing in terms of ample liquidity, low interest rates and the global hunger for higher returns, fact is that two sovereign bonds reached their maturity dates in July (Eurobond of HRK 750 bn and an HRK bond of HRK 6 bn). Interest rates are expected to remain low in 2018. The normalisation of interest rates in Croatia will be gradual, with a more pronounced lag compared to the leading EU Member States. However, it remains essential to continue the favourable trend of fiscal metrics and economic growth. For the time being, both remain promising in the forecasted period and can pave the way for improving the credit rating. However, the path to investment-grade level is long and demanding, and requires improvements in many areas. In the meantime, **the CNB plans to continue pursuing an expansionary monetary policy** and so money market rates are expected to remain at their current historical lows. As Croatia's output gap should close by the end of 2018, and monetary policy in the euro area is expected to tighten, this will gradually be reflected in domestic monetary policy as well. In 2018 the EUR/HRK rate should retain its usual seasonal pattern, and might remain at approximately the same levels on average. Of course, there is still a risk of further slight-but-steady appreciation in the event of a prolonged growth above potential. However, we do not doubt the CNB's commitment to HRK stability.

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

Exchange rate development



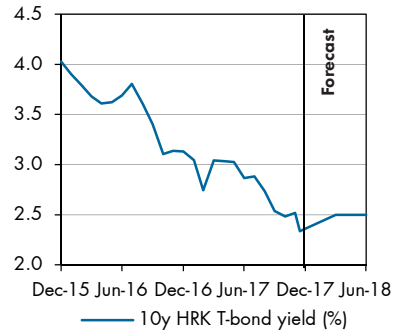
EUR/HRK: 5y high 7.72, 5y low 7.39
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
EUR/HRK	7.55	7.45	7.40	7.45	7.50
Cons.		*7.49*	*7.49*	*7.48*	*7.48*
USD/HRK	6.41	6.48	6.17	6.11	6.05
Cons.		*6.33*	*6.29*	*6.21*	*6.22*

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

HRK yield development (%)



10y HRK T-bond yield: 5y high 6.19, 5y low 2.34
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecast (%)

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
3 month[2]	0.56	0.55	0.55	0.55	0.60
Consensus		0.52	0.50	0.53	0.54

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

Yield forecasts (%)

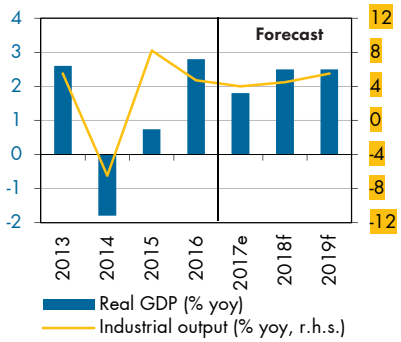
	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
2y T-bond	0.60	0.5	0.6	0.6	0.7
Consensus		n.v.	n.v.	n.v.	n.v.
10y T-bond	2.34	2.5	2.5	2.5	2.5
Consensus		*n.v.*	*n.v.*	*n.v.*	*n.v.*

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

NSB and government on a mission to support the economy

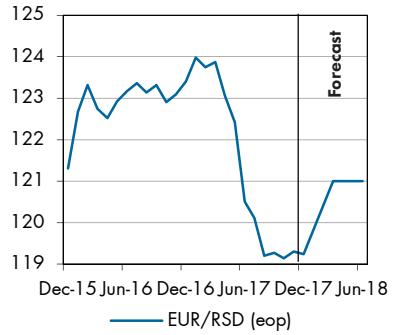
- **New non-financial IMF deal highly likely**
- **Private consumption and investments to support GDP growth**
- **CPI within the corridor**
- **Moderate budget deficit in 2018**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Exchange rate development



EUR/RSD: 5y high 124.06, 5y low 110.33
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

The final review under the 3y precautionary IMF stand-by-arrangement expiring in February 2018 has been closed, and the likelihood of a non-financial Policy Coordination Instrument replacing the SBA is high. Under the IMF deal, the cabinet proved resolute in cutting public debt and the budget deficit considerably. Contrary to the restrained public spending policy in 2017, the **cabinet plans to support economic growth in 2018 by stimulating private consumption** (public sector wages and pension hikes) and by accelerating capital investments. Numerous projects have been planned or launched under the Chinese financial umbrella. That said, the budget deficit was planned at 0.6% of GDP, supported by healthy tax revenues and balanced expenditures. After the USD 770 mn Eurobond repayment, public debt fell from 71.6% to 62.6% of GDP and we assume it will fall further to 60.5% in 2018.

After the two rate cuts in 2017 **we expect a flat base rate of 3.5% in 2018 that will support low interest rates, lending and economic growth.** Inflation will float within the 3.0% +/- 1.5pp corridor, reaching lower rates in H1 2018 due to a high base effect in food and energy prices. Although the IMF and the government predict the economy will boost its growth to 3.5% yoy in 2018, supported by a revival of aggregate demand, infrastructure projects and healthy export growth, we keep our GDP growth estimate at 2.5% for 2018. Traditional postponements in the execution of infrastructure projects together with the protracted privatisation/restructuring of state-owned companies will hinder more upbeat growth. The cancellation of the third early parliamentary elections will certainly weigh positively on the investment climate, with FDI climbing to EUR 1.7 bn; along with the improved export position this will add to the stable EUR/RSD sentiment, with nominal deprecation of only 1.6% yoy for 2018 as a whole.

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

Key economic figures and forecasts

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	34.3	33.1	33.3	35.0	37.8	40.4	42.1
Real GDP (% yoy)	2.6	-1.8	0.7	2.8	1.8	2.5	2.5
Industrial output (% yoy)	5.5	-6.5	8.2	4.7	4.0	4.5	5.5
Unemployment rate (avg, %)	22.1	19.2	17.7	15.3	13.0	11.0	10.5
Nominal industrial wages (% yoy)	1.5	4.0	2.9	4.0	4.0	4.0	3.5
Producer prices (avg, % yoy)	3.6	0.7	0.2	-0.5	1.5	2.5	3.5
Consumer prices (avg, % yoy)	7.9	2.1	1.4	1.2	3.1	2.9	2.9
Consumer prices (eop, % yoy)	2.2	1.7	1.5	1.6	3.0	3.0	3.0
General budget balance (% of GDP)	-5.5	-6.6	-3.7	-1.3	-0.5	-0.8	-1.0
Public debt (% of GDP)	58.8	68.8	74.7	71.6	62.8	60.5	57.5
Current account balance (% of GDP)	-6.1	-6.0	-4.6	-3.9	-4.0	-4.2	-4.0
Official FX reserves (EUR bn)	11.2	10.0	10.4	10.2	10.8	11.5	11.5
Gross foreign debt (% of GDP)	75.4	78.6	81.6	74.2	66.7	63.9	62.5
EUR/RSD (avg)	113.1	117.3	120.7	123.1	121.4	121.2	123.3
USD/RSD (avg)	85.2	88.5	108.8	111.3	106.5	101.0	96.3

Source: National sources, RBI/Raiffeisen RESEARCH

Last minute turnaround related to excise tax on oil

- **Last minute turnaround and adoption of new Law on Excise Tax on Oil**
- **Second tranche of IMF from the EFF could come in Q1 2018**
- **Further continuation of the EFF in 2018 very unrealistic in election year**
- **Weak and uncertain political outlook before 2018 General Elections**

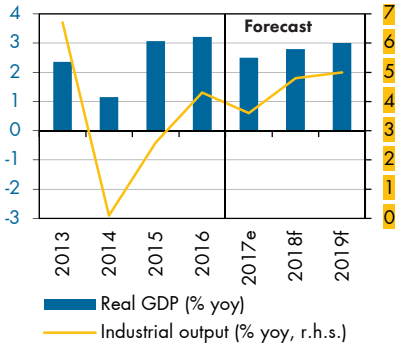
The nationalistic and populist rhetoric escalated in early December, indicating that **pre-election campaigns have already started in the run up to the General Elections in October 2018**, pushing economic and EU accession driven reforms developments into the background.

However, despite all the negative expectations and although declined five times by the State Parliament, causing major political disputes, the Law on Excise Tax on Oil and its products was adopted with new wording in the second week of December. As a reminder, the Law was required and strongly pushed for by the IMF, the European Commission and other European creditors (EBRD, EIB), who are financing infrastructure works on motorway Corridor Vc. Hence we can expect the release of the second tranche by the IMF within the Extended Fund Facility (EFF) during Q1 2018, although we do not think the country will continue with the programme in the election year. Additional funding from the EBRD and EIB for the Corridor Vc construction could be possible in 2018.

So **we have lowered our forecasted real GDP growth rate by 20bp to 2.8% yoy for 2018**, again driven mostly by exports of goods and services (8% yoy), private consumption (1.7% yoy), and partially by gross fixed capital formation (8% yoy). Inflation is expected to be boosted to 1.8% yoy on average by supply-side factors again, with higher imported prices of oil, food and beverages, and transport prices. The unemployment rate should decline further to 18%, mostly as a result of the shrinking labour force and the "brain drain" phenomena visible on the B&H labour market in the past two years. Internal and external imbalances are expected to widen on decelerating exports and rising public spending in the election year. Hence, the current account deficit might reach 5.9% of GDP while the consolidated budget balance should again swing to negative territory of moderate -0.5% of GDP in 2018.

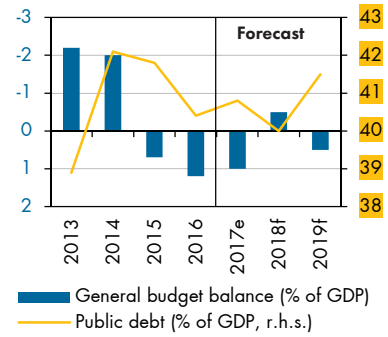
Financial analyst: Ivona Zametica, Raiffeisen BANK d.d., Sarajevo

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: National sources, RBI/Raiffeisen RESEARCH

Key economic figures and forecasts

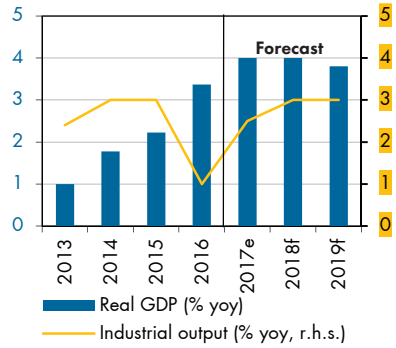
	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	13.7	14.0	14.6	15.3	16.1	17.0	18.0
Real GDP (% yoy)	2.4	1.2	3.1	3.2	2.5	2.8	3.0
Industrial output (% yoy)	6.7	0.1	2.6	4.3	3.6	4.8	5.0
Unemployment rate (avg, %)	27.5	27.5	27.7	25.4	20.5	18.0	16.0
Nominal industrial wages (% yoy)	-0.5	0.3	0.0	0.9	1.4	5.1	6.1
Producer prices (avg, % yoy)	-2.2	-0.2	0.6	-2.3	2.8	2.5	2.3
Consumer prices (avg, % yoy)	-0.1	-0.9	-1.0	-1.1	1.3	1.8	2.0
Consumer prices (eop, % yoy)	-1.2	0.0	-1.3	-0.2	1.4	2.1	2.2
General budget balance (% of GDP)	-2.2	-2.0	0.7	1.2	1.0	-0.5	0.5
Public debt (% of GDP)	38.9	42.1	41.8	40.4	40.8	40.0	41.5
Current account balance (% of GDP)	-5.3	-7.5	-5.5	-4.4	-5.0	-5.9	-6.4
Official FX reserves (EUR bn)	3.6	4.0	4.4	4.9	4.8	5.0	5.3
Gross foreign debt (% of GDP)	52.2	51.8	53.4	54.3	54.8	54.2	53.1
EUR/BAM (avg)	1.96	1.96	1.96	1.96	1.96	1.96	1.96
USD/BAM (avg)	1.47	1.47	1.76	1.77	1.72	1.63	1.53

Source: National sources, RBI/Raiffeisen RESEARCH

Outlook remains positive

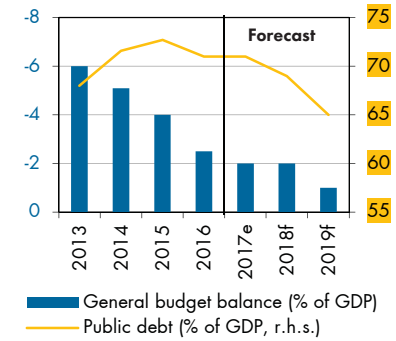
- **Economy to grow at 4% in 2018**
- **Inflationary pressures remain low, monetary policy expansive**
- **Public debt to fall by 2.5% of GDP**
- **Opening of negotiations during H1 2018**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: National sources, RBI/Raiffeisen RESEARCH

Economic growth expanded at 4% on average in H1 2017, compared to 3.5% in 2016. Expected growth remains at 4.0% for the entire year, helped by domestic investment results, the rise in consumption and FDI, and growing tourism. In 2018 the economy is expected to maintain the same growth from 2017, sustained by the **increase in consumption and investments encouraged by low costs of financing, improved confidence and progress in structural reforms**. The recoveries by the main trading partners will have a positive effect on the local economy in 2018 as well. In the low inflationary environment, monetary policy will remain expansionary in 2018. The base rate is at its lowest level since May 2016 of 1.25%, but it will most probably continue for some quarters to come. The higher domestic demand expected in 2018 will result in a higher inflation rate, but the return to the 3.0% target is expected to take place during the first part of 2019.

Fiscal policy will continue to be oriented towards a further reduction of public debt (68.6% of GDP from 71.1% in 2017) and maintaining a low budget deficit of 2.0% of GDP in 2018. The tourism and technology sectors are boosted in the 2018 fiscal package with tax cuts and tax exemptions, but a value-based property tax has also been presented as well as an extended VAT base for small businesses (turnover: ALL 2-5 mn) to increase government revenues and formalise the economy. The **planned public investments will total 5% of GDP in 2018**, and coupled with the USD 1 bn in public-private partnership projects they are expected to have a positive effect on the economy and infrastructure.

The clear mandate of the Socialist government for the next four years provides a good opportunity to make progress with the reform agenda. Albania is in the process of establishing new high judicial institutions as part of the justice reform implementation, which will lead to concrete results in the fight against corruption and organised crime, the key factor for opening negotiations with the EU. The green light to start the process is expected to come during the first half of 2018.

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

Key economic figures and forecasts

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	9.6	10.0	10.2	11.0	12.0	12.8	13.9
Real GDP (% yoy)	1.0	1.8	2.2	3.4	4.0	4.0	3.8
Industrial output (% yoy)	2.4	3.0	3.0	1.0	2.5	3.0	3.0
Unemployment rate (avg, %)	16.0	17.5	17.1	15.2	14.0	14.0	12.5
Nominal industrial wages (% yoy)	8.0	8.0	8.0	3.0	1.9	3.7	3.6
Producer prices (avg, % yoy)	-0.4	-0.5	-2.1	-1.5	1.0	2.0	2.0
Consumer prices (avg, % yoy)	1.9	1.6	1.8	1.3	2.0	2.4	3.0
Consumer prices (eop, % yoy)	1.9	0.7	1.9	2.2	2.5	2.5	3.0
General budget balance (% of GDP)	-6.0	-5.1	-4.0	-2.5	-2.0	-2.0	-1.0
Public debt (% of GDP)	68.0	71.6	72.7	71.0	71.0	69.0	65.0
Current account balance (% of GDP)	-10.7	-12.9	-10.8	-9.1	-9.2	-9.4	-7.9
Official FX reserves (EUR bn)	2.0	2.2	2.9	2.9	3.0	3.0	3.0
Gross foreign debt (% of GDP)	66.2	69.5	73.2	71.7	67.4	64.7	59.8
EUR/ALL (avg)	140.3	140.0	139.7	137.3	134.2	134.6	135.9
USD/ALL (avg)	105.7	105.5	126.0	124.2	117.7	112.1	106.2

Source: National sources, RBI/Raiffeisen RESEARCH

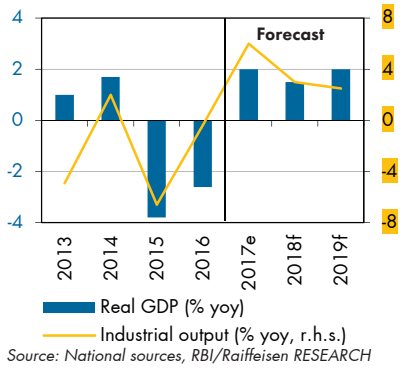
In search of new growth drivers

- **Macroeconomic stability in place, recovery after two-year recession continues**
- **Focus on strengthening private sector, reforms in state sector slow**
- **Short-term liquidity improved thanks to Eurobond, EFSD and Russian loans**
- **Upcoming FX public debt repayments could bring new sovereign bonds in 2018**

Belarus' GDP is expected to rebound by 2% yoy in 2017 after a cumulative decline of 6.4% during the previous two years. The **revival in the Russian economy** as well as April's energy and financial agreements with Russia **and higher oil prices drove a strong 20% increase in the country's exports.** Domestic demand is recovering amidst a solid surge in consumer lending and higher wages. Better policies have helped to achieve macroeconomic stability – strong disinflation, lower CA deficit, stability in the local FX market and a mild devaluation of the local currency. The country's mid-term growth is likely to be in the range of 1.5-2.0% yoy, limited by lagging productivity and competitiveness, and will depend on the performance of the Russian economy. **There's growing recognition of the need for deeper reforms among the local authorities.** A package of documents recently supported by the President is set to improve the business environment – simplifying administrative procedures, bringing tax relief and boosting the digital economy via broader benefits to the country's IT and other high-tech sectors. As part of FX market liberalisation efforts the National Bank intends to cancel the mandatory FX surrender rule, relax controls for FX capital transactions and revoke FX purchase limits for residents. **Further key rate reductions (eight cuts in 2017 from 18% to 11%) are expected** to continue, though at a slower pace depending on CPI dynamics. The regulator managed to contain inflation at an average 6.2% yoy by end-November 2017. The ongoing increase in utility tariffs and the gradual BYN devaluation keep our higher inflationary expectations at an annual 7% in 2017 and 8% going forward. The country's external liquidity is still weak, but improved considerably in 2017 amidst inflows of USD 1.4 bn from a sovereign Eurobond, USD 0.8 bn from EFSD and a Russian loan of USD 0.7 mn. **FX public debt repayments** of an estimated USD 3.7 bn in 2018 (including a USD 0.8 bn Eurobond in January) **might lead to a new sovereign bond issuance next year.**

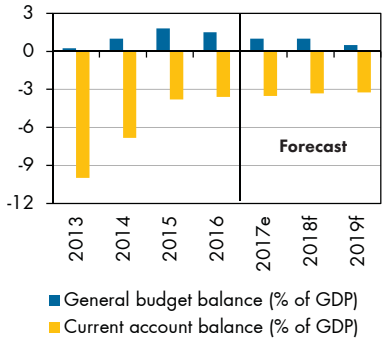
Financial analyst: Natalya Chernogorova, Priorbank Open Joint-Stock Company, Minsk

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget and current account balance



Source: National sources, RBI/Raiffeisen RESEARCH

Key economic figures and forecasts

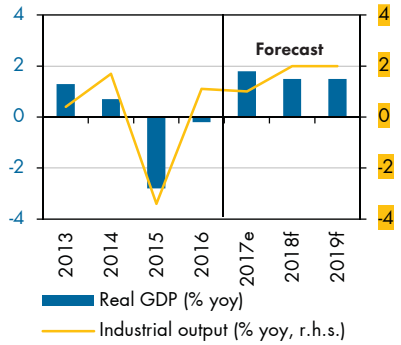
	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	54.9	57.2	49.1	42.9	47.2	45.2	43.4
Real GDP (% yoy)	1.0	1.7	-3.8	-2.6	2.0	1.5	2.0
Industrial output (% yoy)	-4.9	2.0	-6.6	-0.4	6.0	3.0	2.5
Unemployment rate (avg, %)	0.5	0.5	1.0	0.8	1.5	2.0	2.0
Nominal industrial wages (% yoy)	35.2	20.1	7.6	7.3	10.8	10.0	8.0
Producer prices (avg, % yoy)	13.6	12.8	16.8	17.0	12.5	11.0	10.0
Consumer prices (avg, % yoy)	18.3	18.1	13.5	12.0	8.0	7.5	8.0
Consumer prices (eop, % yoy)	16.5	16.2	12.0	10.6	7.0	8.0	8.0
General budget balance (% of GDP)	0.2	1.0	1.8	1.5	1.0	1.0	0.5
Public debt (% of GDP)	32.5	34.1	36.5	39.0	39.0	40.5	40.5
Current account balance (% of GDP)	-10.0	-6.8	-3.8	-3.6	-3.5	-3.3	-3.2
Official FX reserves (EUR bn)	4.8	4.2	3.8	4.7	6.1	5.4	5.3
Gross foreign debt (% of GDP)	51.8	52.6	70.2	79.3	73.4	73.7	73.0
EUR/BYN (avg)	1.18	1.36	1.77	2.20	2.20	2.51	2.88
USD/BYN (avg)	0.89	1.02	1.60	1.99	1.93	2.09	2.25

Source: National sources, RBI/Raiffeisen RESEARCH

Russian economy: one-off factors brighten the picture

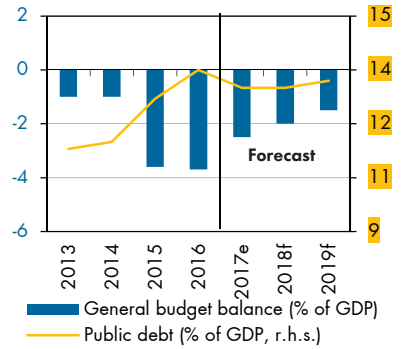
- **Higher GDP growth rates in 2017 achieved mainly due to one-off factors**
- **CPI below CBR's target thanks to one-off factors**
- **Higher FX purchases by MinFin will put pressure on RUB in 2018**
- **Investors in OFZ do not believe in new US sanctions on government debt**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget balance and public debt



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Economic outlook

We have revised our 2017 year-end GDP growth forecast from 1.2% to 1.8% yoy on account of one-off factors, such as a spike in state infrastructure investments in Q2 2018 and restocking. Support is also expected from stable oil prices and the rouble. **Domestic demand recovery** (investments + inventories + consumption) **will be the main driver of GDP**, although there is a lack of fundamental factors to make this recovery fast and sustainable. So we keep our GDP forecast for 2018 at 1.5% yoy. According to Rosstat data, the CPI in November 2017 decreased further to 2.5% yoy (2.7% yoy in October) mainly because of a non-recurring positive factor, disinflation in the food segment, while non-food segment inflation remained stable. We believe that inflation will be around 2.7% yoy at the end of 2017 following seasonal inflation growth in December. Going forward in 2018 we expect that the one-off factors that brought inflation to historically low levels will gradually fade. Moreover, a **slow but continuous recovery of consumption as well as pre-election social expenditure will contribute to faster inflation.** So the CPI is likely to be above the CBR's target of 4% at year-end 2018. In our baseline scenario we forecast that the CBR will maintain its moderate approach to monetary easing in 2018. Apart from the inflationary risks, which the regulator also admits, inflation expectations remain unanchored and the RUB is likely to come under pressure following the introduction of the new budget rule. The higher RUB-denominated oil prices throughout 2017 have resulted in higher budget revenues and a lower budget deficit (around RUB 2 tn). In 2018 the MinFin expects a deficit of RUB 1.3 tn due to 1) growth of non-oil & gas revenues, which will result in total revenue growth of RUB 538 bn, and 2) a cut in government spending by RUB 200 bn. Although the current budget plan does not imply an increase in the **oil price in 2018**, it is **likely that it will be revised upwards in the near future** (for Urals above 50 USD/bbl). This should help increase budget revenues significantly. At the same time, the high possibility

Key economic figures and forecasts

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	1,678.8	1,551.7	1,223.8	1,160.5	1,384.8	1,344.1	1,289.8
Real GDP (% yoy)	1.3	0.7	-2.8	-0.2	1.8	1.5	1.5
Industrial output (% yoy)	0.4	1.7	-3.4	1.1	1.0	2.0	2.0
Unemployment rate (avg, %)	5.5	5.2	5.6	5.5	5.3	5.3	5.3
Average gross wages (% yoy)	12.3	8.3	4.2	7.9	6.0	6.0	6.0
Producer prices (avg, % yoy)	3.4	6.1	12.4	4.0	7.5	6.5	6.5
Consumer prices (avg, % yoy)	6.8	7.8	15.6	7.1	3.6	3.5	4.3
Consumer prices (eop, % yoy)	6.5	11.4	12.9	5.4	2.7	4.3	4.3
General budget balance (% of GDP)	-1.0	-1.0	-3.6	-3.7	-2.5	-2.0	-1.5
Public debt (% of GDP)	11.3	11.5	12.7	13.5	13.0	13.0	13.2
Current account balance (% of GDP)	1.5	3.1	5.1	1.7	2.0	3.8	2.8
Official FX reserves (EUR bn)	369.8	318.5	339.1	358.1	343.2	346.8	348.5
Gross foreign debt (% of GDP)	32.7	29.1	37.9	39.0	29.3	25.8	22.6
EUR/RUB (avg)	42.3	51.0	68.0	74.1	66.4	73.6	81.8
USD/RUB (avg)	31.9	38.6	61.3	67.0	58.3	61.4	63.9

Source: National sources, RBI/Raiffeisen RESEARCH

of budget expenditure growth (especially during the presidential elections) may keep the final estimate of the budget deficit close to the planned levels.

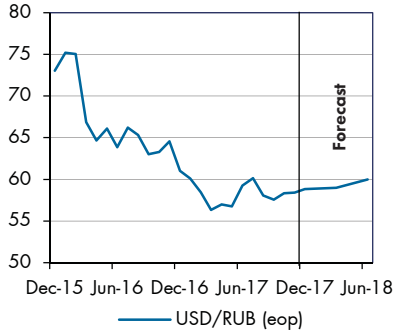
Financial analysts: Stanislav Murashov, AO Raiffeisenbank, Moscow

Financial market outlook

The positive price development of the OFZ market recently is likely to have been driven by local factors. The CBR admitted that during Q2-Q3, in response to the new regulation, pension fund managers had to increase their OFZ position while decreasing their investment in credit institution assets. We note that **since September, yields on short and medium-term OFZ have been falling**, unlike other local GEM bonds. The opposite dynamic in OFZ could be driven by the afore-mentioned investors after they received their funds from the banks under rehabilitation (FC Otkritie and B&N). At the MinFin re-offering auctions there is solid demand for OFZs, whereas foreigners, we believe, are staying on the sidelines due to sanction-related concerns. The OFZ market implies that the probability of sanctions against Russian sovereign debt is close to zero (which is arguable, in our view). If this risk materialises, however, it will result in a significant downward market correction (by 100-150bp for 10y OFZs); if it does not, the upside is rather small, as further key rate cuts have widely been priced in. **We prefer front-end OFZs, which could produce gains on our end-March recommendation horizon, especially for EUR-based investors** due to favourable effects from our EUR/USD projections. Assuming that sanctions are not implemented, in the medium term the CBR will continue cutting the key rate down to 6%, and the yield on 10y OFZ will reach a long-term equilibrium at 6.5-7%. Supported mostly by the oil price rebound, the RUB as a commodity-related currency managed to ignore the depreciation trend observed in many EM currencies in H2 2017 when the USD/RUB fluctuated within quite a narrow range of 57-61. The performance of the RUB-denominated Brent price that rocketed from RUB 2,700 to RUB 3,800 per barrel suggests an actual rouble weakening driven by a shortage of FCY liquidity on the local market, and comes in anticipation of the **new budget rule that is expected to be implemented from January 2018**. To recap, the key difference from the old rule is the linking of FX interventions to the USD-denominated oil price. This change will allow for the avoidance of both excessive RUB appreciation (in the case of capital inflows in a high oil price environment) and excessive RUB depreciation (in the case of capital outflows). From 2018 it is planned that the amount of FCY purchases will be calculated as the difference between revenues actually received and the revenues which would be received under the base oil price (URALS at USD 40.8/bbl in 2018) and the actual FX rate. We estimate that the new rule will significantly increase the amount of FX purchases (at least 2.5x if Brent is at USD 60) and put pressure on the RUB, which could partly be offset by capital inflows on fears of new sanctions against some Russian businessmen.

Financial analysts: Denis Poryvay, AO Raiffeisenbank, Moscow

Exchange rate development



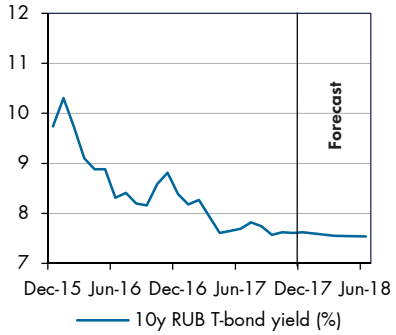
USD/RUB: 5y high 84.24, 5y low 29.87
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
EUR/RUB	69.29	67.9	72.0	79.3	79.4
Cons.		*68.1*	*69.0*	*71.0*	*71.1*
USD/RUB	58.84	59.0	60.0	65.0	64.0
Cons.		*59.0*	*58.6*	*58.2*	*59.0*

[1] 5:00 p.m. (CET)
Source: Thomson Reuters, 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 (%)

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
Key rate	7.75	7.50	7.00	6.75	6.75
Consensus		*7.7*	*7.4*	*7.2*	*7.0*
3 month[2]	8.33	7.6	7.4	7.2	7.2
Consensus		n.v.	n.v.	n.v.	n.v.

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

Yield forecasts (%)

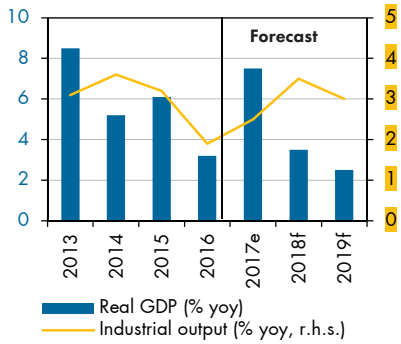
	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
2y T-bond[2]	7.20	7.3	7.1	7.13	7.0
Consensus		*7.2*	*7.1*	*6.8*	*6.8*
10y T-bond[2]	7.62	7.6	7.5	7.4	7.3
Consensus		*7.3*	*7.3*	*7.2*	*7.2*

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

Extraordinary growth hand in hand with record high inflation

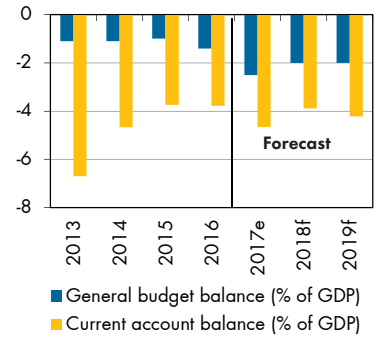
- **GDP growth easily beats market expectations, putting upwards pressure on forecasts for 2018**
- **Turkish lira and surge in food prices push inflation to highest level since 2003, opening the door for rate hikes**
- **Despite significant TRY undervaluation, risks for the lira remain elevated**
- **Short-term relief potential for TURKGBs should TRY stabilise**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget and current account balance



Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Economic outlook

As expected, **GDP growth in Q3 exceeded the figures for the preceding two quarters**, outpacing them by more than 5pp, i.e. **11.1% yoy compared to 5.3-5.4% yoy in H1.** However, this extraordinary growth can largely be attributed to a statistical base effect following the contraction in Q3 2016 after the attempted military coup. Nonetheless, an increase of this magnitude exceeds consensus forecasts. The main contributors to the dynamics have been a surge in private consumption expenditure (growth of 11.7% yoy), exports (17.2% yoy) and fixed capital investment (12.4% yoy). Going forward, such high rates of growth are not sustainable and we expect the economy to cool down in 2018, but **we still raise our forecasts for GDP growth from 2.5% to 3.5%.** Growth could come in even higher as multiple elections (including presidential elections) are scheduled for 2019, and the Turkish authorities have a strong incentive to keep the economy running at high steam until these are over. However, employing very expansionary policies can also be risky as an overheating economy could turn into a subsequent slowdown or even recession.

Inflation in Turkey hit a fourteen-year high at 13.0% yoy in November. The main drivers behind this surge in inflation seem to be the pass-through from TRY depreciation versus the major currencies as well as an uptick in food inflation. Even though Turkish policymakers switched to a cautious tightening mode recently, the **independence of the central bank remains questionable** given the ongoing pressure from local politics. However, the most prominent risks for the Turkish lira markets will come from the expected repricing of the Fed's monetary policy outlook, with market participants underestimating the future path of rate hikes according to current market pricing. The related temporary strength of the USD vs EMFX is likely to weigh on Turkish assets, at least given the elevated private-sector debt levels denominated in US dollars. Nevertheless, we assume that the TCMB has to keep

Key economic figures and forecasts*

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	714.7	703.8	773.4	780.1	754.1	750.2	742.0
Real GDP (% yoy)	8.5	5.2	6.1	3.2	7.5	3.5	2.5
Industrial output (% yoy)	3.1	3.6	3.2	1.9	2.5	3.5	3.0
Unemployment rate (avg, %)	9.0	9.9	10.3	10.0	10.3	10.0	10.0
Nominal industrial wages (% yoy)	6.0	n.v.	n.v.	n.v.	n.v.	n.v.	n.v.
Producer prices (avg, % yoy)	4.5	10.2	5.3	4.3	16.0	12.0	9.0
Consumer prices (avg, % yoy)	7.5	8.9	7.7	7.8	11.0	9.5	8.0
Consumer prices (eop, % yoy)	7.4	8.2	8.8	7.0	12.0	8.5	7.5
General budget balance (% of GDP)	-1.1	-1.1	-1.0	-1.4	-2.5	-2.0	-2.0
Public debt (% of GDP)	36.2	35.0	34.0	32.0	33.0	32.0	32.0
Current account balance (% of GDP)	-6.7	-4.7	-3.7	-3.8	-4.7	-3.9	-4.2
Official FX reserves (EUR bn)	95.1	105.2	101.7	100.6	89.0	80.6	75.8
Gross foreign debt (% of GDP)	41.0	43.0	46.4	47.5	47.7	46.7	45.3
EUR/TRY (avg)	2.53	2.90	3.02	3.34	4.13	4.68	5.29
USD/TRY (avg)	1.91	2.19	2.73	3.02	3.62	3.90	4.13

** new revisions to national accounts data not included*
Source: National sources, RBI/Raiffeisen RESEARCH

monetary conditions tight despite widespread expectations of inflation returning to single-digit figures in the course of **2018 (we assume average yearly consumer price inflation of around 9% yoy).**

The current account deficit grew in November by 0.6pp compared to the preceding month, indicating an end or at least an interruption of the recovery process seen in the past few years. With the **deficit currently totalling 4.7% of GDP**, Turkeys' dependency on capital inflows from abroad seems to be increasing, and therefore raises its **vulnerability to any deterioration in external conditions.**

Financial analyst: Andreas Schwabe, CFA, RBI Vienna

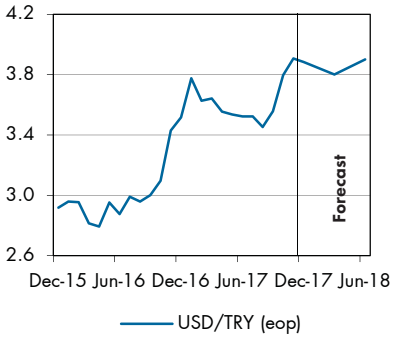
Financial market outlook

After witnessing another phase of **significant depreciation in early Q4 2017**, the Turkish lira has **recently** seen **some stabilisation** regarding the speculation of monetary policy tightening by the Turkish Central Bank (TCMB). Then again, this stabilisation could turn out to be short-lived if the TCMB is tempted to loosen conditions again after a temporary tightening. Assuming that the TCMB at least succeeds in calming market fears and with the expectation of a decline in inflation rates below 10% in Q1 2018, we see some moderate potential for additional lira stabilisation in the first quarter of 2018. This is also underpinned by the fact that the lira is currently significantly undervalued against the USD. However, the **overall political risk remains elevated and difficult to predict.** A renewed rise in inflation rates for Q2-Q4 2018, ongoing political jitters and the global rate normalisation process should then contribute to a lira setback for the remainder of 2018. **We expect the USD/TRY will exceed 4.0 in the course of H2 2018**, but do not predict a renewed phase of extreme lira weakening as was the case in Q1 and Q4 2017.

In line with our FX baseline scenario, **TURKGBs may continue in relief mode** as long as the central bank manages to prevent the TRY exchange rate from depreciating further. This is more likely the tighter monetary conditions are kept by the TCMB, despite the temptation of the aforementioned easing expected in the CPI headline inflation rate towards single-digit territory in the course of 2018. In this scenario, real rates would turn positive in early 2018, increasing the attractiveness of lira assets. A gradual simplification towards a more orthodox monetary policy toolkit would help restore confidence in the Turkish central bank, especially in an environment of normalising global rates, which calls for a buffer for Turkish lira markets. However, earlier statements concerning monetary policy simplification have fallen silent in recent times, the TCMB did not even emphasise this option in its recent monetary policy outlook for 2018. That said, **in the short term we would consider re-entering the Turkish local debt market for short-term speculative reasons.** A normalisation of the considerably inverted TURKGB curve to some degree is also possible in our view, albeit to a limited extent only given the need to keep short-end rates high in order to maintain a positive carry.

Financial analysts: Wolfgang Ernst, CEFA, Stephan Imre, RBI Vienna

Exchange rate development



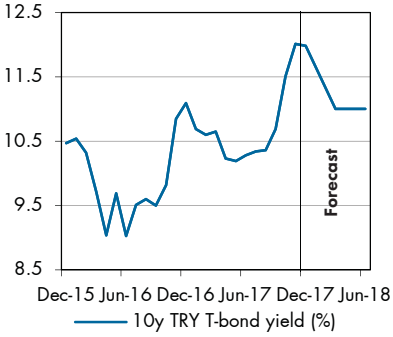
USD/TRY: 5y high 3.96, 5y low 1.75
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Exchange rate forecasts

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
EUR/TRY	4.57	4.37	4.68	4.88	4.96
Cons.		*4.54*	*4.74*	*4.88*	*5.00*
USD/TRY	3.88	3.80	3.90	4.00	4.00
Cons.		*3.95*	*3.95*	*4.00*	*4.03*

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

TRY yield development (%)



10y TRY T-bond yield: 5y high 12.78, 5y low 6.02
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Interest rate forecasts (%)

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
Key rate	8.00	8.00	8.00	8.00	8.00
Consensus		*8.05*	*8.05*	*8.05*	*8.00*
3 month[2]	14.60	13.00	13.20	13.50	14.00
Consensus		*12.51*	*12.20*	*12.04*	*11.95*

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

Yield forecasts (%)

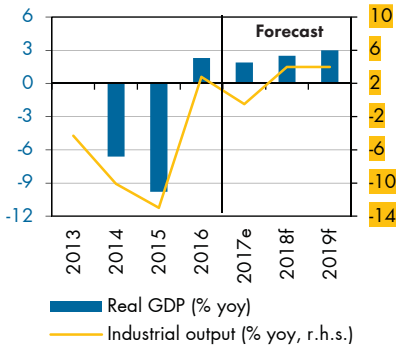
	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
2y T-bond	13.16	12.3	12.5	13.0	13.5
Consensus		*11.2*	*10.8*	*10.3*	*10.3*
10y T-bond	11.98	11.0	11.0	11.5	12.0
Consensus		*10.8*	*10.8*	*10.6*	*10.9*

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

Stable economic performance, but growing political risk

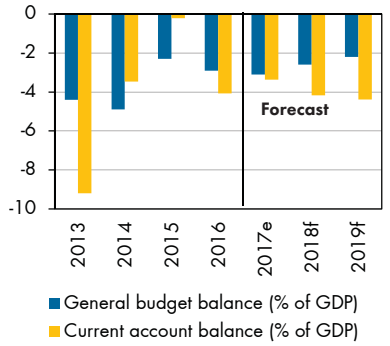
- **Moderate growth of 2-3% in 2018 to continue**
- **Inflation starting to slow down, but still above the target**
- **Relatively high gross international reserves**
- **Upcoming elections and growing political pressure as the major risks**

Real GDP (% yoy)



Source: National sources, RBI/Raiffeisen RESEARCH

Budget and current account balance



Source: National sources, RBI/Raiffeisen RESEARCH

Ukraine's economy has been showing moderately strong growth in 2017 on the back of a revival of business activity and improvements in social well-being. We increase our conservative 2017 GDP growth estimate by 0.4pp to 1.9% yoy. Nevertheless, given the pending reforms and growing political uncertainty, we decreased our **GDP forecast for 2018 from 3% yoy to 2.5% yoy.** Due to the economic blockade of Donbas, industrial production dynamics were flat in January-October 2017, but we expect an improvement to +4% yoy in 2018. **Inflation has started decelerating** owing to the strong base effect (significant hike in tariffs in 2016), but the Central Bank's **target of 6-10% yoy will not be met in 2017.** However, we believe inflation can return to the regulator's goal in 2018 on the back of a prudent monetary policy and the fading negative shocks of this year, returning below 8% yoy by December 2018. In terms of risks we see a threat to price stability from the sharp increase in social standards (minimum wage, pensions, etc.), which is partly motivated by the upcoming elections. Meanwhile, given the economic stabilisation we see the current account deficit deepening to about 3.4% of GDP in 2017 and 4.2% in 2018.

Gross international reserves reached USD 18.9 bn in November, giving the Central Bank enough resources to stabilise the market in the event of growing volatility. The traditional hike in UAH liquidity by the end of the year may increase pressure on the FX market in December 2017 and January 2018, but in Q2 2018 and Q3 2018 we expect to see a seasonal strengthening of the UAH. Nevertheless, we **estimate a USD/UAH rate of 28.50 by the end of 2018**. At the same time, the reforms in Ukraine have stalled, which is delaying the next IMF tranche. Given the significant debt payments in the upcoming years and the elections in 2019, Ukraine only has a limited amount of time to improve cooperation with the Fund and attract sufficient funding.

Financial analysts: Sergii Drobot, Raiffeisen Bank Aval Public Joint Stock Company, Kiev

Key economic figures and forecasts

	2013	2014	2015	2016	2017e	2018f	2019f
Nominal GDP (EUR bn)	135.3	99.9	81.7	84.3	96.4	100.0	98.0
Real GDP (% yoy)	0.0	-6.6	-9.8	2.3	1.9	2.5	3.0
Industrial output (% yoy)	-4.3	-10.1	-13.0	2.8	-0.5	4.0	4.0
Unemployment rate (avg, %)	7.8	9.7	9.5	9.7	9.5	9.0	9.0
Nominal industrial wages (% yoy)	7.9	6.0	20.5	23.6	35.0	15.0	10.0
Producer prices (avg, % yoy)	-0.1	17.1	36.0	20.5	26.2	13.1	5.8
Consumer prices (avg, % yoy)	-0.2	12.1	48.7	13.9	14.4	9.2	5.6
Consumer prices (eop, % yoy)	0.5	24.9	43.3	12.4	13.2	6.5	5.5
General budget balance (% of GDP)	-4.4	-4.9	-2.3	-2.9	-3.1	-2.6	-2.2
Public debt (% of GDP)	40.7	52.9	72.3	76.1	70.1	62.9	59.5
Current account balance (% of GDP)	-9.2	-3.5	-0.2	-4.1	-3.4	-4.2	-4.4
Official FX reserves (EUR bn)	14.8	6.2	12.2	14.7	16.3	17.6	17.0
Gross foreign debt (% of GDP)	79.3	95.2	130.9	121.7	102.4	93.3	88.5
EUR/UAH (avg)	10.8	15.9	24.3	28.3	30.3	33.3	37.0
USD/UAH (avg)	8.2	12.0	22.0	25.6	26.6	27.7	28.9

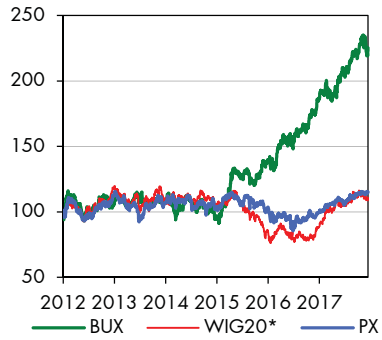
Source: National sources, RBI/Raiffeisen RESEARCH

A bumpy start to the new year

- **Signs of overheating on the developed stock markets increase risk of consolidation**
- **Equity markets supported by very robust economic conditions**
- **Expansive monetary policy by local central banks remains in place**
- **Still no normalisation of political relations with Russia**

In Q4 2017, the CEE equity markets which we follow were roughly on par with the established stock markets in Western Europe. With the exception of Poland, the performance in CEE can be described as moderately positive. In general, economic conditions on both sides of the Atlantic are still extremely good. However, the recent highs registered for leading indicators hardly leave any room for significant improvements. As for politics, we do not expect any major turbulence during the first quarter of 2018. In the USA, we expect that an agreement will soon be reached to avert a looming US government shutdown. Moreover, US President Trump can now finally show some success with the agreement on the long-awaited tax reform in the USA. With regard to monetary policy and liquidity, sentiment may gradually be tempered, in light of the further reduction in the Fed's balance sheet and the current outlook for interest rate hikes, and depending on the development of inflationary pressure. In Europe, on the other hand, there is little cause for worry about the turnaround in monetary policy, as the bond purchase programme will be cautiously reduced and initial interest rate increases should only come in 2019. Despite the very good overall conditions, we anticipate a rather bumpy start to the new year in 2018, due to the various tendencies towards overheating and the positive newsflow that has been widely priced in. Nevertheless, taking a one-year perspective, we maintain our positive view.

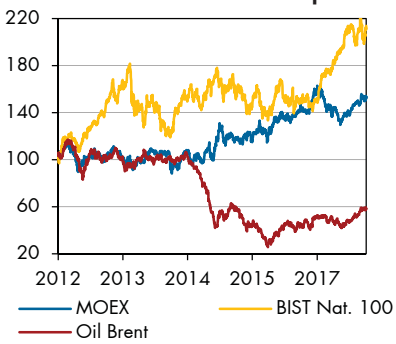
CE core equity indices



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

As of the end of November, the **MICEX** was officially renamed the **MOEX**. After a poor start to 2017, the leading index in Moscow was able to recoup almost all of its losses in the second half of the year. Naturally, this was also due to the strong recovery in the oil price, which recently advanced to the highest level since the mid of 2015, on the back of gradually weakening data on stocks and expectations of robust demand. Another catalyst for prices was the November announcement that the production cap agreement between OPEC and non-OPEC states would be extended. For the time being, however, we see a bit too much good news discounted in oil prices, and consequently there may be some profit-taking in Q1. As the year progresses though, the oil price should then move swiftly again towards the levels which have been seen recently. In parallel with this, the beginning of the year should be rather subdued for the MOEX. For 2018 as a whole, however, we expect this factor to be moderately supportive. In terms of politics, the presidential elections will be coming into focus in Q1, along with

MOEX & BIST 100 Nat. vs oil price



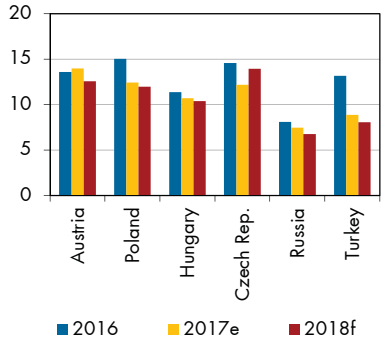
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Value matrix stock markets

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

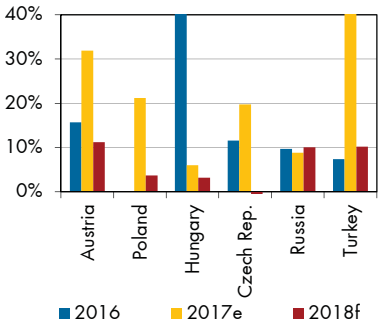
1 (4) denotes highly positive (negative) influence on the market. All factors are weighted equally. Assessment refers to a 3-month period. Figures in brackets reflect our former assessment.
Source: RBI/Raiffeisen RESEARCHSource: RBI/Raiffeisen RESEARCH

P/E ratios in comparison



Source: Thomson Reuters, IBES, Bloomberg, RBI/Raiffeisen RESEARCH

Earnings growth



Source: Thomson Reuters, IBES, Bloomberg, RBI/Raiffeisen RESEARCH

the future course of sanctions. With regard to the former, an election victory for Putin is certain. Sectoral sanctions recently were extended by the EU for another six months, while the tightening of US sanctions that has been initiated could pop up again from time to time as a negative factor. The moderate economic recovery in Russia should continue to provide support for Russian equities, in particular as the decline in inflation will allow the central bankers to continue the cycle of interest rate cuts. From the perspective of valuations, we believe that the MOEX is still trading at too much of a discount compared to the other Emerging Markets. This is also the case as analysts' consensus figures for projected earnings growth rates for this year and next year look very solid (2017e: 8.8%, 2018f: 10.0%). In light of the predominantly positive factors, we project benign developments on the Russian equity market for 2018 as a whole, whereas the beginning of the year should be subdued. Q1: **Hold**.

In Q4 2017, the Polish **WIG 30** equity index weakened slightly, but still ranks in first place among the CE-3 countries since the beginning of the year. Economic activity has recently been significantly better than expected, prompting us to upgrade our estimate for 2017 GDP growth from 4.0% to 4.4% and our forecast for 2018 growth from 3.2% to 4.1%. Despite the clear increase in wage pressure stemming from the tightening labour market, the rise in inflation has been moderate so far, and accordingly we only expect to see an initial interest rate hike during the second half of 2018. The political disputes with the EU continue, and the replacement of the previous prime minister Beata Szydlo with the former finance and economics minister Mateusz Morawiecki will probably not make much of a difference. On a fundamental basis, the 2017e aggregate earnings growth anticipated by consensus was able to rise by four percentage points to 21.2%. Looking to 2018f, we currently expect the pace of earnings growth to decelerate to 3.7%. The resulting valuation of (PER 2018f: 12.0) appears moderate to us and should offer good support on the downside in the event of falling prices. Q1: **Hold**.

The **Czech** equity market index **PX** posted mild increases in Q4 2017. Macroeconomic conditions remain very robust, with the GDP estimate for 2017 revised slightly upwards by 0.1 percentage points to 4.4%. While economic performance is clearly above potential and rests on a firm basis, we believe there is limited potential for the strong dynamics to continue rising, as a result of the very high level of employment. Consequently, we project GDP growth of 3.3% for 2018. In order to keep inflation under control, the Czech central bank intends to allow the CZK to gradually appreciate, which ultimately may also lead to additional rate hikes. Following the general elections in October, the formation of the new government is almost complete, especially since the election winner Andrej Babis has already been appointed as prime minister. So far, however, the new government has neither a coalition partner nor the necessary support for a minority government. 2017e aggregate earnings growth for the index have now risen to

Stock market indicators

	Earnings growth			Price/earnings ratio			Dividend yield
	2016	2017e	2018f	2016	2017e	2018f	2017e
ATX	15.7%	31.9%	11.2%	13.6%	14.0%	12.6%	2.9%
WIG 30	0.2%	21.2%	3.7%	15.0%	12.4%	12.0%	2.3%
BUX	68.1%	6.1%	3.2%	11.4%	10.7%	10.4%	2.7%
PX	11.6%	19.7%	-12.7%	14.6%	12.2%	13.9%	5.2%
MOEX	9.7%	8.8%	10.0%	8.1%	7.4%	6.8%	5.5%
BIST Nat. 100	7.4%	48.5%	10.2%	13.2%	8.9%	8.0%	4.0%

Source: Thomson Reuters, IBES, Bloomberg, RBI/Raiffeisen RESEARCH

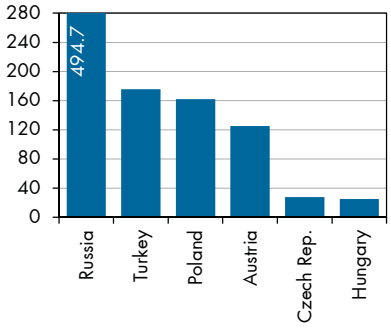
19.7%, whereas current projections point to a decline in earnings of 12.7% for 2018f. The resulting 2018f PER of 13.9 leaves the index with a valuation that is just barely still in moderate territory. We remain optimistic over a one-year horizon, but would not rule out a small consolidation at the start of the year. Q1: **Hold**.

The **Hungarian** index **BUX** also posted mild gains in the past quarter. Macroeconomic conditions remain very positive, and consequently we have left our GDP forecasts unchanged for 2017e at 3.8% and for 2018f at 3.6%. Although the rate of inflation is gradually rising as a result of the increasing tightness of the labour market and the related wage pressure, the Hungarian central bank continues to pursue a clearly expansive policy (QE programme scheduled to run from 2018) to prevent appreciation of the forint. On an adjusted, aggregate basis, the anticipated increase in earnings in 2017e of 0.1% has now improved to 6.1%, and for 2018f we are currently projecting growth of 3.2 % in earnings. The resulting PER of 10.4 for 2018f appears relatively attractive to us. Q1: **Hold**.

The **BIST 100** index is still the strongest market in our equity market universe, having posted a gain of 40% since the beginning of the year. The economic data had already been pointing to acceleration and the very strong GDP growth figures delivered for Q3 have confirmed this development. Although the economic performance looks impressive, one must also keep in mind that it has been accompanied by very high inflation recently (November 2017: 13% yoy) and a steadily weakening currency. Moreover, politics is a factor of uncertainty that must be reckoned with disputes with the EU and the USA. The expected aggregate earnings growth of the securities in the index is estimated at 10.2% for 2018f, and in light of the economic growth this figure is quite plausible. The 2018f PER calculated on this basis amounts to 8.0, which looks relatively cheap. Although the Turkish equity market clearly still looks like a "Buy" based on the fundamental aspects, we abstain from this due to the unpredictable political risk situation. Q1: **Hold**.

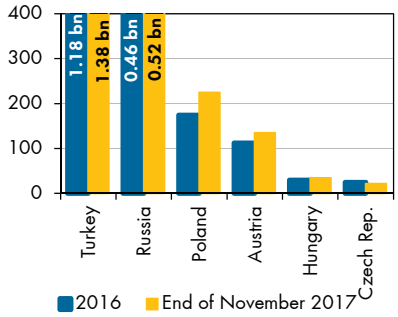
Financial analysts: Andreas Schiller, CFA, Christian Hinterwallner, CEFA, RBI Vienna

Market capitalisation overview



In EUR bn; cut off for data : 12/14/2017
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Avg. daily turnover (EUR mn)



Source: FESE, WFE, RBI/Raiffeisen RESEARCH

Index estimates

	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18	Recommendation
ATX	3,311	3,400	3,520	3,270	3,600	**HOLD**
Performance		2.7%	6.3%	-1.2%	8.7%	
Range		3,000 - 3,700	3,100 - 3,800	2,900 - 3,800	2,900 - 3,900	
MICEX	2,794	2,830	2,980	2,730	2,960	**HOLD**
Performance		1.3%	6.7%	-2.3%	6.0%	
Range		2,500 - 3,100	2,500 - 3,200	2,500 - 3,200	2.,500 - 3,200	
WIG 30	38,616	39,400	41,200	38,000	41,000	**HOLD**
Performance		2.0%	6.7%	-1.6%	6.2%	
Range		34,800 - 42,200	35,500 - 44,100	34,200 - 44,100	34,200 - 43,900	
BUX	1,065	1080	1120	1040	1120	**HOLD**
Performance		1.4%	5.1%	-2.4%	5.1%	
Range		1,000 - 1,200	1,000 - 1,200	900 - 1,200	900 - 1,200	
PX	2,152	2,210	2,290	2,140	2,340	**HOLD**
Performance		2.7%	6.4%	-0.6%	8.7%	
Range		1,900 - 2,400	2,000 - 2,500	1,900 - 2,500	1,900 - 2,600	
BIST Nat. 100	109,666	112,500	115,500	113,500	115,000	**HOLD**
Performance		2.6%	5.3%	3.5%	4.9%	
Range		98,700 - 120,400	101,300 - 123,600	102,200 - 123,600	102,200 - 123,100	

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

Upside potential looking thin after robust gains

- **Economy firing on all cylinders**
- **Strong outlook for earnings**
- **Valuations have increased, but still look attractive compared to fixed-income alternatives**

Value matrix*

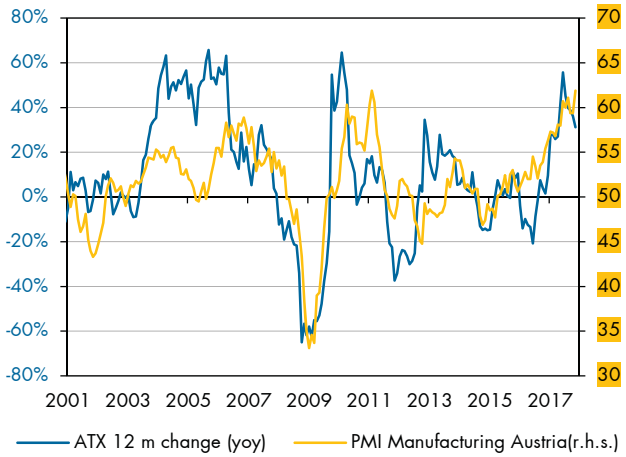
Domestic business activity		1	(1)
Exports	OECD excl. Eastern Europe	1	(1)
	Eastern Europe	1	(1)
	Asia	1	(1)
Corporate profits		1	(1)
Key sectors		2	(2)
Valuation		2	(2)
Interest rates / yields		2	(2)
Exchange rates		2	(2)
Foreign equity markets		2	(1)
European liquidity		1	(1)
Technical outlook		2	(2)

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 **Austrian equity market** performed exceptionally well in 2017, and the appreciation of the euro was only able to briefly undermine this. Since the start of the year, the ATX index has registered a gain of around 26%, making it one of the strongest performers in the entire euro area. The outperformance by the ATX was mainly driven by the robust economic activity in Austria and its neighbouring economic region. Another positive factor was that the index heavyweight OMV was able to significantly outperform the global energy sector. The Vienna Stock Exchange also registered the first IPO in many years, reflecting the upbeat sentiment on the Austrian equity market.

For 2018, we expect to see further advances by the ATX, although the pace of these gains will be increasingly bumpy. The projection that the bull market will basically continue is based on the **development of earnings and economic growth**, both of which are expected to be strong. There have recently been several indications that the economy is humming along at a much healthier clip than it has been in quite some time. The generally very reliable purchasing managers' index for the manufacturing sector continues to fluctuate around its record highs. Consequently, it should come as no surprise if some weaker data are released here and there in the coming months. Such developments could then trigger a more subdued start to the new year. Nevertheless, there are also many signs of very robust economic conditions in the euro area and in the Eastern European economies, which are important sales markets for many Austrian companies. In light of these good conditions, we have boosted our growth forecasts again. For 2017, we now expect GDP growth to be +3.2% (previously: +2.8%) and 2018 should also feature growth which is well higher than the potential rate (now projected at +2.6% versus the previous figure of +2.2%). This growth will continue to be powered by private consumption and corporate investment. Exports and the construction industry are also fuelling growth. Austria thus

Purchasing managers quite optimistic



Source: Thomson Reuters, Markit, RBI/Raiffeisen RESEARCH

Sector structure of the ATX

Sector	Company	Weight
Financials	BAWAG, Erste Group, Raiffeisen Bank International, Uniqa, Vienna Insurance Group	35.4%
Energy	OMV, SBO	17.8%
Materials	Lenzing, voestalpine	14.0%
Industrials	Andritz, Österreichische Post, Wienerberger, Zumtobel	13.8%
Real Estate	BUWOG, CA Immobilien, Immofinanz, S IMMO	13.8%
Utilities	Verbund	2.6%
Telecommunication	Telekom Austria	2.0%
Consumer Staples	Agrana	0.6%

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

continues to enjoy robust economic performance, after years of underperformance.

The ECB's **monetary policy** is another important factor. The central bank's plans to reduce the bond purchase programme were met with little grumbling. The monetary policy bias remains extremely expansive, and we expect that the first interest rate hike will only occur in early 2019. Therefore, we see little upside potential for yields on the secondary market. This keeps **refinancing costs** for companies **low** and the equity market looking more attractive than the bond market in terms of valuations (current risk premium of around 700 basis points).

From an absolute perspective, however, due to the robust price increases the **valuation** of the ATX has risen substantially over the last year, which means that the market is no longer so cheap. According to our estimates, the Austrian benchmark index will feature an adjusted price-earnings ratio of 14 for 2017.

We expect continued support from **corporate earnings.** Based on our adjusted aggregate earnings estimations for 2017, an increase of >30% is anticipated. In 2018, profits should once again be in the low double-digit percentage zone.

Summary: On the whole, the strong economic activity and robust earnings growth, paired with the ongoing expansive monetary policy, suggest that the **upward trend** in the key index for Vienna's stock exchange **should continue.** Nevertheless, the increase in valuations indicates that there is less and less upside potential for additional gains. Moreover, worries about US interest rates should have a negative impact on the Austrian market over the course of the year. **Q1: Hold.**

Financial analyst: Christian Hinterwallner, CEFA, RBI Vienna

Valuation and forecasts

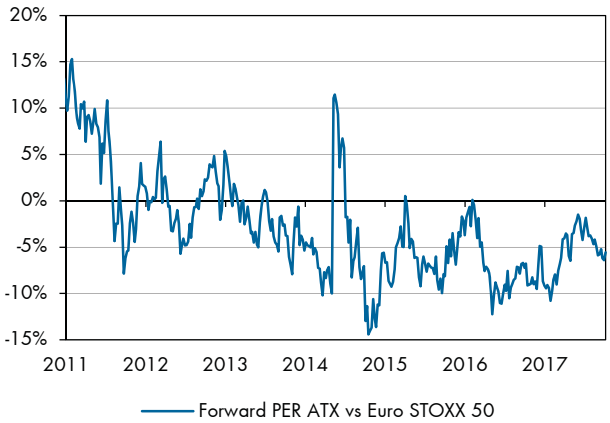
	14-Dec[1]	Mar-18	Jun-18	Sep-18	Dec-18
ATX forecast	3,311	3,400	3,520	3,270	3,600
Expected performance		2.7%	6.3%	-1.2%	8.7%
Range		3,000 - 3,700	3,100 - 3,800	2,900 - 3,800	2,900 - 3,900

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

Equity risk premium still attractive

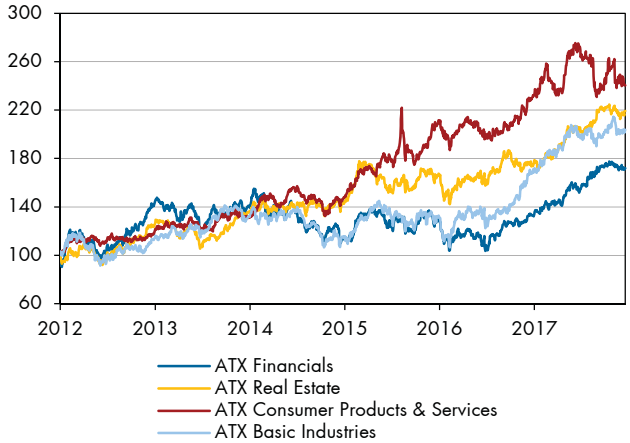
Source: Thomson Reuters, IBES, RBI/Raiffeisen RESEARCH

ATX discount melting



Source: Thomson Reuters, IBES, RBI/Raiffeisen RESEARCH

Sector indices in comparison



rebased to 100
Source: Bloomberg, RBI/Raiffeisen RESEARCH

Stock Markets: Signs of weakening uptrend

ATX

.ATX, 15/12/2017, 06:10 a.m. (CET), 5y high: 3,445, 5y low: 1,957
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

ATX

Last: 3,311 **NEUTRAL**

As our first target 3,350 got hit, yet not the second one at 3,570, the trend-channel's upper band. Instead the upward-trend (since 01/07/2016) is being tested-out, and a sell-signal at 3,250 thus is likely to get triggered. Nevertheless, a topside breakout at 3,380 would be considered as a bullish confirmation.

Position:

Buy	3,380	-> 3,440 – 3,570
Sell	3,250	-> 3,150 – 3,055

BIST National 100

.XU100, 15/12/2017 07:55 a.m. (CET), 5y high: 114,166, 5y-low: 61,189
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

BIST National 100

Last: 109,666 **BULLISH**

Triggering of the stop at 104,500 has paid-off as the consolidation phase has not ended since. The trend-channel's upper band at 120,000 would again be considered the target once 115,100 gets crossed; else a drop through 106,000 would signal a decline that should continue with 99,200 (-> 90,980).

Position:

Buy	115,100 -> 120,000
Stop	106,000 -> 102,330 – 99,210…

BUX

.BUX, 15/12/2017, 06:30 a.m. (CET), 5y high 40,274, 5y low 15,687
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

BUX

Last: 38,616 **NEUTRAL**

Our target 39,220 had been hit before triggering of the stop 37,600. In order to renew bullishness the 6-weeks moving average would have to get crossed at 39,080. As long as the like is lacking the still not impossible bearish reversal pattern might get confirmed at 38,180.

Position:

Long	-> 39,220 – 41,620…
Stop	37,600

BET

Last: 7,587 **NEUTRAL**

Our stop got triggered at 8,300, and the sell-limit 7,500 has been put to the test now. As this week shows a Hammer line a bullish signal at 8,090 cannot be fully excluded, although the overall pattern's appearance is bearish still. So, in case the buy-signal does not get triggered the bearish trend should get confirmed at 7,400 instead.

Position:

Buy	8,090	-> 8,340 – 8,510…
Sell	7,400	-> 7,215 – 6,855

BET

.BETI, 15/12/2017 11:30 a.m. (CET), 5y high: 8,769, 5y-low: 4,840
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

MOEX

Last: 2,152 **~BULLISH**

Since hitting of the target at 2,180 the market has begun to consolidate. Nevertheless, headroom stretches towards 2,305 still as the upward-trend (since 15/06/2017) keeps on providing support, although it is being tested thoroughly. Setbacks towards 2,040 cannot be fully excluded. Sell from 2,030 (-> 1,960 – 1,850)

Position:

Long	-> 2,190 – 2,305
Stop	2,040

MOEX

.MCX, 15/12/2017 11:45 a.m. (CET), 5y high: 2,285, 5y-low: 1,237
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

WIG 30

Last: 2,793 **NEUTRAL**

Subsequent to the marking of the current trend-high at 2,954 the expected retracement to 2,800 has set in. AS the latter target has been undershot downward potential stretches towards the major support at 2,600. A further decrease down to there might get confirmed at 2,720, while a buy-signal at 2,820 cannot be excluded by now.

Position:

Buy	2,820	-> 2,880 – 2,945
Sell	2,720	-> 2,600 – 2,520

WIG 30

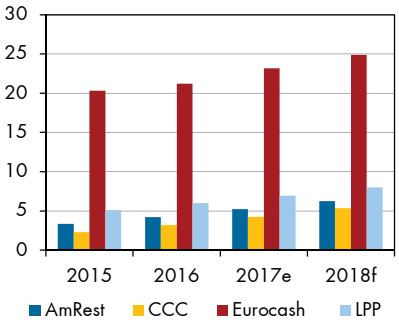
.WIG30, 15/12/2017 07:27 a.m. (CET), 5y high: 2,954, 5y-low: 1,879
Source: Thomson Reuters, RBI/Raiffeisen RESEARCH

Financial analyst: Robert Schittler, CEFA, RBI Vienna

Looming Sunday trade ban in Poland

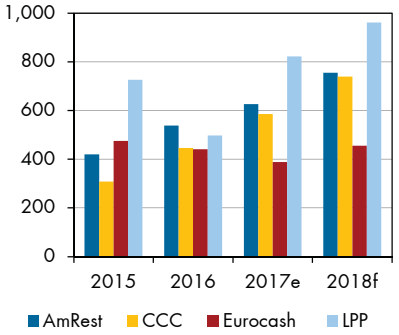
- **Progressively increasing Sunday shopping restrictions planned for 2018-20e**
- **We reckon with a catalysing effect on e-commerce**
- **We favour Eurocash and CCC as those with the least to lose from the regulation**

Polish consumer sector - Revenues*



** PLN bn*
Source: Companies, Raiffeisen Centrobank estimates

Polish consumer sector - EBITDA*



** PLN mn*
Source: Companies, Raiffeisen Centrobank estimates

While the consumption environment remains attractive in Poland, benefitting consumer companies, we highlight the risk from the looming Sunday trade ban. The regulation envisions progressively advancing limitations on Sunday shopping. Starting in March 2018f shopping would be restricted on two Sundays every month, excluding Sundays before key holidays. For 2019f the proposal envisions a shopping ban on three Sundays a month, progressively moving to a shopping ban on all Sundays by 2020f. Polish trade unions have been putting pressure on the government to implement a full Sunday shopping ban as soon as possible, and it is thus possible that the regulations will be tweaked. The proposal excludes small owner-operated shops as well as specific locations like train stations and hotels. It currently seems that online shopping should not be restricted by the regulations, which we expect to result in increased customer interest in that channel.

We believe that a meaningful portion of apparel sales are spontaneous impulse-driven purchases which would otherwise not happen if the customer did not browse through the store, and hence while we expect a large proportion of these potential sales to move to other days of the week, we do not expect a complete recovery of all potential Sunday purchases. We thus expect apparel retailers, to increase their focus on the online channel in 2018f. According to data from the Polish statistics office, 30% of adult Poles purchased clothing online in the last twelf months. With regard to FMCG and groceries we reckon with large format stores, such a hypermarkets, to be impacted the most given expected larger queues on Saturdays resulting in people increasing their purchases during the week, which is likely to benefit formats such as neighbourhood discounters and supermarkets.

In our coverage universe we expect the most benign impact of the regulation on Eurocash and CCC. Some of Eurocash's clients, being small owner-operated stores, are likely to be allowed to operate their retail locations on all Sundays and Eurocash franchise supermarkets are likely to capture a larger portion of the Sunday traffic migrating to other days of the week than some competitors. Meanwhile CCC, focussing on mainstream footwear, should be able to preserve the majority of its sales, which are often driven by the weather situation. Furthermore CCC has a very strong online business, which it expects to contribute 20% of its sales in FY 2018f.

Financial analyst: Jakub Krawczyk, Raiffeisen Centrobank

The comeback of E&P players

- **Extension of production cut agreement to support oil price stabilisation**
- **2018e E&P capex seen higher in the USA and internationally**
- **We favour Lotos and MOL due to their balanced exposures to upstream and downstream**

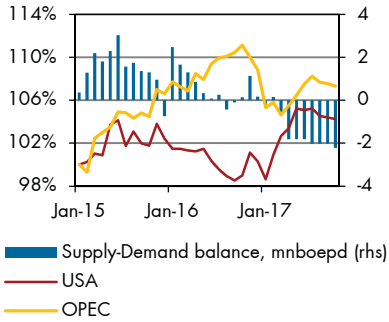
The extension of the OPEC production cut agreement until the end of 2018 combined with the IEA's forecast of global demand growth of 1.2% in 2018e should keep the oil price within a narrower range. Lower oil price volatility is seen supportive for a recovery of E&P spending, which we expect to grow not only in the USA, but also internationally. Consequently, we reckon that the upstream players might be encouraged to allocate higher capex to their E&P activities, which should add new barrels of crude oil in the medium to long term. Moreover, we expect the strengthening oil prices combined with a gradual decrease of the gas output in North European countries (i.e. due to a natural decline of production) to support natural gas prices.

We reckon that a healthier refining environment could last for longer provided that the oil price stays below the three-digit level, while the regional consumption of motor fuels continues to improve on the back of stronger economic activity. In our opinion, the regional refiners should be in a better shape now, having improved their efficiency as well as the yields of white products as a result of massive investments over the last 5-7 years. As long as the oil price stays way below the three-digit level and motor fuel consumption continues to grow even at a moderate pace, we would expect the NWE refining margin to stay between USD 5.0-6.0/ bbl, which is in line with the 2007-17e average. Petchem producers could face lower petchem earnings due to a higher cost of feedstock (i.e. naphtha). We reckon that in our universe PKN Orlen might be less impacted due to a higher weight of high-margin petchem products.

In our coverage universe we prefer Lotos and MOL. We favour Lotos due to its strong exposure to the domestic fuel market, where it is enjoying a healthy level of in-land premium. Additionally, the expected completion of the Gdansk refinery upgrade should improve Lotos's realised refining margins by ca. USD 2.0/bbl. MOL is another of our favourite stocks due to its balanced exposure to upstream and downstream, which should enable it to benefit from both stronger crude oil and gas prices as well as robust consumption of motor fuels in the CEE region.

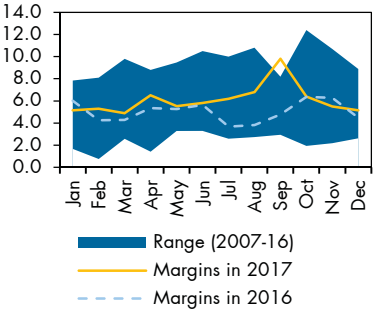
Financial analyst: Oleg Galbur, Raiffeisen Centrobank

USA/OPEC production growth*



** re-based to Jan-15*
Source: IEA Oil market report

NWE refining margins, USD/bbl



Source: Thomson Reuters

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Investment recommendation	Column A Basis: All recommendations for all financial instruments (last 12 months)	Column B Basis: Recommendations for financial instruments of all issuers, for which special services were rendered in the last 12 months
Buy recommendations	37.6%	42.7%
Hold recommendations	42.4%	32.4%
Sell recommendations	20.0%	4.8%

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Disclosure aspects

Company	Disclosure
Lotos	-
MOL	5, 6
PKN	-
CCC	3
Eurocash	3
Evraz Group SA	-
CREDIT BANK OF MOSCOW	5
Vnesheconombank	-
Sberbank	-
OMV	3

Bonds

Local currency government bonds: Recommendations concerning financial instruments or issuers (disseminated during a period of 12 month prior to this publication), which differ from recommendations made in this publication*

	CZ		CZK	HU		HUF	PL		PLN	RO		RON	RU		RUB	TR		TRY
Date	2y	10y		2y	10y		2y	10y		2y	10y		2y	10y		2y	10y	
15/12/2016	H	H	H	H	B	H	H	B	H	H	H	H	B	H	H	S	S	H
24/01/2017	I	I	I	I	I	I	I	I	I	I	I	I	H	I	I	H	H	I
24/02/2017	I	I	I	I	I	I	I	H	I	I	I	I	S	S	S	I	I	I
15/03/2017	I	B	B	I	H	I	I	I	I	I	I	I	H	H	H	I	S	I
27/04/2017	I	I	I	I	I	I	I	I	S	I	I	I	B	B	I	I	H	S
06/06/2017	I	H	I	I	B	I	I	B	H	I	I	I	I	I	I	B	I	H
20/06/2017	I	I	H	I	H	I	I	I	B	S	S	I	I	I	I	I	I	I
24/08/2017	S	S	S	I	I	S	I	I	H	H	H	H	I	I	I	I	I	I
07/09/2017	I	I	H	B	I	H	I	I	I	I	I	I	I	I	I	I	I	I
21/09/2017	I	I	B	I	I	I	I	I	I	I	I	I	I	I	I	I	I	I
12/10/2017	H	H	H	I	I	I	I	I	I	I	I	I	I	I	I	I	I	B
25/10/2017	I	I	I	H	I	I	I	I	I	I	I	I	I	I	I	H	I	H
30/11/2017	I	I	I	I	I	I	I	I	I	I	I	I	H	H	I	I	I	I
15/12/2017	I	I	B	I	I	I	I	I	B	I	I	I	B	B	I	I	I	I

** recommendations based on absolute expected performance in LCY; B: Buy, H: Hold, S: Sell, I: no change, - no coverage*

Sovereign Eurobonds: Recommendations concerning financial instruments or issuers (disseminated during a period of 12 month prior to this publication), which differ from recommendations made in this publication*

	BG		HR		CZ		HU		KZ		LT		PL	
Date	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD
15/12/2016	H	–	H	H	H	–	H	H	–	B	H	B	H	H
24/01/2017	I	–	I	I	I	–	I	I	–	H	B	I	I	I
24/02/2017	I	–	B	I	I	–	I	I	–	I	I	I	I	I
15/03/2017	I	–	I	I	I	–	I	I	–	I	H	H	I	I
27/04/2017	I	–	H	I	I	–	I	B	–	I	S	I	B	I
06/06/2017	B	–	I	B	I	–	I	H	–	I	H	I	H	I
20/06/2017	I	–	I	H	I	–	I	I	–	I	I	I	B	I
07/09/2017	H	–	I	I	I	–	I	I	–	B	I	I	H	I
21/09/2017	I	–	I	I	I	–	I	I	–	I	I	I	I	I
25/10/2017	I	–	I	I	I	–	I	I	–	H	I	I	I	I
30/11/2017	I	–	I	I	I	–	I	I	–	I	S	S	S	S
15/12/2017	I	–	I	I	I	–	I	I	–	I	I	I	I	I

** recommendations based on absolute expected performance, i.e. expected spread change; B: Buy, H: Hold, S: Sell, I: no change, - no coverage*

Sovereign Eurobonds: Recommendations concerning financial instruments or issuers (disseminated during a period of 12 month prior to this publication), which differ from recommendations made in this publication*

	RO		RU		RS		TR		UA		BY		MK	
Date	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD	EUR	USD
15/12/2016	H	H	H	S	–	B	H	H	–	S	–	S	H	–
24/01/2017	I	I	I	I	–	H	I	I	–	I	–	H	I	–
24/02/2017	I	I	I	I	–	I	I	I	–	I	–	I	I	–
15/03/2017	B	B	I	H	–	I	I	I	–	I	–	I	B	–
27/04/2017	H	H	I	I	–	I	I	I	–	I	–	B	H	–
06/06/2017	I	I	I	I	–	S	I	I	–	H	–	H	B	–
20/06/2017	I	I	I	I	–	I	B	B	–	I	–	I	I	–
07/09/2017	I	I	I	I	–	H	I	I	–	B	–	I	I	–
21/09/2017	I	I	I	I	–	I	I	I	–	I	–	B	I	–
25/10/2017	I	I	I	I	–	I	I	I	–	I	–	I	I	–
30/11/2017	I	I	I	I	–	S	I	I	–	I	–	H	I	–
15/12/2017	I	I	I	I	–	I	H	H	–	H	–	I	I	–

** recommendations based on absolute expected performance, i.e. expected spread change; B: Buy, H: Hold, S: Sell, I: no change, - no coverage*

Corporate Credits

Recommendations history for 12 months

Evraz Group SA			
ISIN	Date of past recommendation	Company	Recommendation
XS1533915721	24/11/2017	Evraz Group SA	Buy

CREDIT BANK OF MOSCOW			
ISIN	Date of past recommendation	Company	Recommendation

Vnesheconombank			
ISIN	Date of past recommendation	Company	Recommendation
XS0524610812	24/11/2017	Vnesheconombank	Buy
XS0893212398	24/11/2017	Vnesheconombank	Buy
XS0524610812	08/11/2017	Vnesheconombank	Buy
XS0893212398	08/11/2017	Vnesheconombank	Buy

Sberbank			
ISIN	Date of past recommendation	Company	Recommendation
XS0743596040	24/11/2017	Sberbank	Buy
XS0743596040	13/07/2017	Sberbank	Buy

Equities

Recommendation history

Lotos: 5y high: PLN 67.8, 5y low: PLN 23.068294				
10.01.2011*	Rating	Target Price	Prev. day's close	Upside
05.12.2017	Buy	73.00	55.04	32.6%
20.09.2017	Hold	60.50	60.00	0.8%
18.08.2017	Buy	60.00	51.30	17.0%
19.04.2017	Hold	57.00	52.48	8.6%
12.09.2016	Hold	30.50	28.34	7.6%
04.05.2016	Hold	32.50	30.50	6.6%
10.02.2016	Buy	29.50	25.13	17.4%

MOL: 5y high: HUF 3,328, 5y low: HUF 1,338.75				
01.02.2002*	Rating	Target Price	Prev. day's close	Upside
08.11.2017	Buy	3,700	3,220	14.9%
16.08.2017	Buy	3,200	2,868	11.6%
14.03.2017	Buy	3,038	2,581	17.7%
23.02.2017	Hold	2,975	2,628	13.2%
12.09.2016	Hold	2,313	2,161	7.0%
01.06.2016	Buy	2,275	1,938	17.4%
19.05.2016	Hold	2,275	2,013	13.0%
29.03.2016	Reduce	1,938	1,981	-2.2%
10.02.2016	Hold	1,750	1,714	2.1%

PKN: 5y high: PLN 134, 5y low: PLN 36.88				
01.02.2002*	Rating	Target Price	Prev. day's close	Upside
23.10.2017	Buy	135.00	121.70	10.9%
05.07.2017	Hold	118.00	110.35	6.9%
21.03.2017	Reduce	98.00	107.05	-8.5%
19.01.2017	Hold	88.00	85.75	2.6%
12.09.2016	Buy	76.50	64.00	19.5%
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%

** Initiation date*

Recommendation history

Eurocash: 5y high: PLN 65.64, 5y low: PLN 26.6				
17.08.2011*	Rating	Target Price	Prev. day's close	Upside
09.08.2017	Buy	41.00	34.11	20.2%
16.11.2016	Hold	39.00	34.35	13.5%
21.09.2016	Hold	46.00	41.80	10.0%
02.07.2016	Hold	49.00	46.34	5.7%
18.02.2016	Reduce	53.00	56.25	-5.8%

CCC: 5y high: PLN 298, 5y low: PLN 67				
04.04.2012*	Rating	Target Price	Prev. day's close	Upside
26.09.2017	Buy	340.00	289.30	17.5%
23.02.2017	Buy	250.00	216.80	15.3%
16.11.2016	Buy	215.00	181.00	18.8%
21.09.2016	Buy	200.00	167.80	19.2%
05.04.2016	Hold	155.00	152.80	1.4%
18.02.2016	Buy	155.00	129.40	19.8%

** Initiation date*

WIG20: 5y high: 2628.3, 5y low: 1674.57
BUX: 5y high: 40273.66, 5y low: 15686.69

Coverage universe recommendation overview

	buy	hold	reduce	sell	suspended	UR
Universe	54	59	10	2	2	3
Universe %	42%	45%	8%	2%	2%	2%
Investment banking services	29	33	6	0	1	2
Investment banking services %	41%	46%	8%	0%	1%	3%

Source: Raiffeisen Centrobank, rounding differences may occur

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Raiffeisen Bank International AG

Registered Office: Am Stadtpark 9, 1030 Vienna

Postal address: 1010 Vienna, POB 50

Phone: +43-1-71707-0 **Fax:** + 43-1-71707-1848

Company Register Number: FN 122119m at the Commercial Court of Vienna

VAT Identification Number: UID ATU 57531200

Austrian Data Processing Register: Data processing register number (DVR): 4002771

S.W.I.F.T.-Code: RZBA AT WW

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Global Raiffeisen RESEARCH Team: Peter Brezinschek, FA* (Leitung)

Austria: Raiffeisen Bank International AG (RBI AG)

Research Sales and Operations
Werner Weingraber (Head)
Birgit Bachhofner
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Kathrin Kořinek
Andreas Mannsparth
Bostjan Petac
Aleksandra Srejic
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Retail Research Manager
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Helge Rechberger, FA*

Market Strategy/Quant Research
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Economics/Fixed Income/FX Research
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Lydia Kranner, FA*
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Gottfried Steindl, FA*
Martin Stelzeneder, FA*

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Hannes Loacker, FA*
Johannes Mattner, FA*
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Leopold Salcher, FA*
Christoph Vahs, FA*

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Ruslan Gadeev, FA*
Eva-Maria Grosse, FA*
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Martin Kutny, FA*
Werner Schmitzer, FA*
Jürgen Walter, FA*

Company Research:
Raiffeisen Centrobank AG
Bernd Maurer, FA*(Head)

Christian Bader, FA*
Oleg Galbur, FA*
Jakub Krawczyk, FA*
Stefan Maxian, FA*
Dominik Niszcz, FA*
Markus Remis, FA*
Teresa Schinwald, FA*
Jovan Sikimic, FA*
Arno Supper, FA*

Albania:
Raiffeisen Bank Sh.A.
Dritan Baholli, FA*
Valbona Gjeka, FA*

Belarus:
Priorbank JSC
Natalya Chernogorova, FA*
Vasily Pirogovsky, FA*

Bosnia & Herzegovina:
Raiffeisen Bank dd Bosna i Hercegovina
Ivona Zametica, FA*
Srebrenko Fatusic, FA*

Bulgaria:
Raiffeisenbank (Bulgaria) Sole-owned Joint Stock Company
Emil S. Kalchev, FA*

Croatia:
Raiffeisenbank Austria d.d.
Zrinka Zivkovic Matijevic, FA*
Marijana Cigic, FA*
Elizabeta Sabolek-Resanovic, FA*
Ana Turudic, FA*

Czech Republic:
Raiffeisenbank a.s.
Helena Horska, FA*
Jakub Červenka, FA*
Milan Frydrych, FA*
Lenka Kalivodova, FA*
František Táborský, FA*

Hungary:
Raiffeisen Bank Zrt.
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Gergely Pálffy, FA*
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Poland:
Raiffeisen Polbank
Dorota Strauch, FA*
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Romania:
Raiffeisen Bank S.A.
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Catalin Diaconu, FA*
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Russia:
AO Raiffeisenbank
Anastasia Baykova, FA*
Denis Poryvay, FA*
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Stanislav Murashov, FA*
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Serbia:
Raiffeisen banka a.d.
Ljiljana Grubic, FA*

Slovakia:
Tatra banka, a.s.
Robert Prega, FA*
Juraj Valachy, FA*
Boris Fojtik, FA*
Tibor Lörincz, FA*

Ukraine:
Raiffeisen Bank Aval JSC
Sergii Drobot, FA*

* FA ... Financial analyst

Raiffeisen Bank International AG

Markets & Investment Banking

Raiffeisen Bank International AG
Group Capital Markets: Nicolaus Hagleitner T: +43 1 71707-1467
Investment Banking Products: Matthias RennerT: +43 1 71707-2123

RB International Markets (USA) LCC
Stefan Gabriele T: +1 212 835-2328

AL: Raiffeisen Bank Sh.a.
Christian Canacaris T: +355 4 2275519-2629

BH: Raiffeisen Bank d.d. Bosna i Hercegovina
Reuf Sulejmanovic T: +387 33 287-449

BG: Raiffeisenbank (Bulgaria) EAD
Boyan Petkov T: +359 2 91985-635

BY: Priorbank JSC
Tresary: Svetlana N. Gulkovich T: +375 17 2899-080
Investment Banking: Oleg Leontev T: +375 17 2899-251

CZ: Raiffeisenbank a.s.
Milan Fischer T: +420 234 40-1145

HR: Raiffeisenbank Austria d.d.
Robert Mamic T: +385 1 4695-076

HU: Raiffeisen Bank Zrt.
Gabor Liener T: +36 1 484-4304

KO: Raiffeisen Bank Kosovo J.S.C.
Berat Isa T: +38 1 3822 2222-229

PL: Raiffeisen Polbank
Miroslaw Winiarczyk T: +48 22 585-3710

RO: Raiffeisen Bank S.A.
Aurelian Mihailescu T: +40 213 061-221

RS: Raiffeisen Banka a.d.
Capital Markets:
Branko Novakovic T: +381 11 2207-131
Joko-Lola Tomic T: +381 11 2207-145

RU: AO Raiffeisenbank
Capital Markets: Sergey Shchepilov T: +7 495 721-9977
Investment Banking: Oleg Gordienko T: +7 495 721-9900

SK: Tatra banka, a.s.
Peter Augustin T: +421 2 5919-1313

UA: Raiffeisen Bank Aval JSC
Vladimir Kravchenko T: +380 44 49542-20

Raiffeisen CENTROBANK AG

CEO: Wilhelm Celeda T: +43 1 51520-402
Head of Global Equity Markets: Klaus della Torre T: +43 1 51520-472
Head of Company Research: Bernd Maurer T: +43 1 51520-706
Head of Investment Services: Andrea Lerch T: +43 1 51520-411

Commercial Banks

Raiffeisen Bank International AG, Vienna
Corporate Customers: Joseph Eberle T: +43 1 71707-1487
Financial Institutions: Axel Summer T: +43 1 71707-1476

RBI London Branch
Matthias Renner T: +44 20 7933-8001

RBI Beijing Branch
Terence Lee T: +86 10 8531-9007

RBI Singapore Branch
Klaus Krombass T: +65 6305-6024

International Desk

AL: Raiffeisen Bank Sh.a.
Jorida Zaimi T: +355 4 2381-445

AT: Raiffeisen Bank International AG
Rudolf Lercher T: +43 1 71707-3537

BG: Raiffeisenbank (Bulgaria) EAD
Irena Krentcheva T: +359 2 9198-5826

BH: Raiffeisen Bank d.d. Bosna i Hercegovina
Vildana Sijamhodzic T: +387 33 287-283

BY: Priorbank JSC
Natalya Selickaya T: +375 172 899-355

CZ: Raiffeisenbank a.s.
Roman Lagler T: +420 234 40-1728

HR: Raiffeisenbank Austria d.d.
Wolfgang Woehry T: +385 1 4566-462

HU: Raiffeisen Bank Zrt.
Gaspar Tiszai T: +36 1 484-4421

KO: Raiffeisen Bank Kosovo J.S.C.
Valerija Mustafa T: +38 1 38 222 222-413

PL: Raiffeisen Polbank
Krzysztof Lubkiewicz T: +48 22 347-7155

RO: Raiffeisen Bank S.A.
Aurel Voicescu T: +40 764 601-847

RS: Raiffeisen banka a.d.
Sofija Davidovic T: +381 11 220-7807

RU: AO Raiffeisenbank
Maria Maevskaya T: +7 495 775-5230

SK: Tatra banka, a.s.
Mirco Ribis T: +421 2 5919-1846

UA: Raiffeisen Bank Aval
Victoria Masna T: +380 44 23023-44