

| Instant Reaction |

EcoAlert

Accelerating inflation increased the chance of a hike; the koruna strengthens



Viktor Zeisel
(420) 222 008 523
viktor_zeisel@kb.cz

Consumer price indices - May 2017

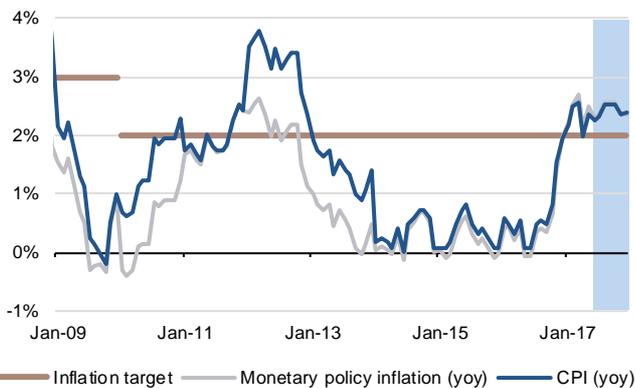
| | Current | KB forecast | Consensus |
|-------------------------|---------|-------------|-----------|
| Consumer prices (% mom) | +0.2 | -0.2 | -0.1 |
| Consumer prices (% yoy) | +2.4 | +2.0 | +2.2 |

Source: Bloomberg, CZSO, Economic & Strategy Research, Komerční banka

Domestic inflation remains above the CNB's target as it surged to 2.4% in May. Though the CNB expected even higher inflation in its last forecast, we can assume today's figure is an upside surprise given the developments in April. Today's inflation reading provides further support to our call that the CNB will hike this year. The markets have been reflecting the increasing probability of a hike as the koruna appreciated to EUR/CZK26.2 initially after the reading was released.

The price level increased 0.2% compared with April. Though fuel prices recorded a decrease of 1.1% mom, their drop was offset by an increase of core prices. Their growth accelerated to 0.2% mom. Their dynamics were supported by the rise in food prices by 0.5% mom. Regulated prices remained unchanged.

Inflation accelerated and is set to remain above the CNB's target



Source: CZSO, CNB, Macrobond, Economic & Strategy Research, Komerční banka

CPI sub-indices

| | mom | yoy |
|-----------------------------------|-------------|-------------|
| Total | 0.2% | 2.4% |
| Food and non-alcoholic beverages | 0.4% | 4.5% |
| Alcoholic beverages, tobacco | 0.6% | 1.3% |
| Clothing and footwear | 0.2% | 1.4% |
| Housing, water, energy, fuel | 0.3% | 1.7% |
| Furnishings, households equipment | -0.1% | -0.2% |
| Health | 0.6% | 3.3% |
| Transport | -0.3% | 4.1% |
| Post and telecommunications | -0.2% | -0.1% |
| Recreation and culture | 0.1% | 1.1% |
| Education | 0.0% | 2.2% |
| Restaurants and hotels | 0.3% | 5.7% |
| Miscellaneous goods and services | -0.4% | 0.9% |

Source: CZSO, Macrobond, Economic & Strategy Research, Komerční banka

Core inflation regained its role as the driver of price dynamics when it climbed to 2.2%. Moreover, core inflation included a 2.8% rise in prices of services, which corroborates the view that price growth is due to the strengthening purchasing power of households resulting in domestic demand pressures. Regulated prices supported inflation in May as the base effect stemming from lower gas prices fades as gas for consumers became cheaper in May 2016. Yet, this effect was mitigated by a deceleration of fuel price growth while food prices maintained solid dynamics at 4.5%.

Though the CNB expected May's inflation at 2.6% in its last forecast, we believe that, given April's reading, today's figure is an upside surprise. The EUR/CZK rate reacted by appreciating and moved below EUR/CZK 26.20 for a moment. Today's statistics corroborate our call that the CNB is set to increase interest rates this year. Our forecast suggests the central bank will act at its November meeting.

An even stronger koruna will not halt the core inflation increase



Source: CZSO, Bloomberg, Macrobond, Economic & Strategy Research, Komerční banka

Consumer price inflation should remain above the 2% CNB's target. Core inflation will ensure that as it will be supported by accelerating wage growth, inducing higher purchasing power of households. These trends are suggested by wage growth readings released last week and a report on wages in industry issued on Tuesday. Inflation will be only impeded by the easing of food and fuel price dynamics. Overall, inflation should reach 2.3% on average this year.

KB ECONOMIC & STRATEGY RESEARCH

Chief Economist and Head of Research
Jan Vejmelek, Ph.D., CFA
 (420) 222 008 568
 jan_vejmelek@kb.cz

Economists
Viktor Zeisel
 (420) 222 008 523
 viktor_zeisel@kb.cz

Equity Analysts
Miroslav Frayer
 (420) 222 008 567
 miroslav_frayer@kb.cz

Marek Dřimal
 (420) 222 008 598
 marek_drimal@kb.cz

Richard Miřátský
 (420) 222 008 560
 richard_miratsky@kb.cz

David Kocourek
 (420) 222 008 569
 david_kocourek@kb.cz

Jana Steckerová
 (420) 222 008 524
 jana_steckerova@kb.cz

SG IN CENTRAL AND EASTERN EUROPE

Chief Economist of SG Poland
Jaroslav Janecki
 (48) 225 284 162
 jaroslav_janecki@sgcib.com

Head of Research of Rosbank
Yury Tulinov, CFA
 (7) 495 662 13 00 (ext. 14836)
 yury.tulinov@rosbank.ru

Chief Economist of BRD-GSG
Florian Libocor
 (40) 213 016 869
 florian.libocor@brd.ro

Head of Fin. Markets Research BRD-GSG
Carmen Lipara
 (40) 213 014 370
 carmen.lipara@brd.ro

Economist
Ioan Mincu
 (40) 213 014 472
 george.mincu-radulescu@brd.ro

Equity Analyst
Laura Simion, CFA
 (40) 213 014 370
 laura.simion@brd.ro

SG GLOBAL ECONOMICS RESEARCH

Head of Global Economics
Michala Marcussen
 (44) 20 7676 7813
 michala.marcussen@sgcib.com

Euro area
Anatoli Annenkov
 (44) 20 7762 4676
 anatoli.annenkov@sgcib.com

North America
Stephen Gallagher
 (212) 278 4496
 stephen.gallagher@sgcib.com

Asia Pacific
Klaus Baader
 (852) 2166 4095
 klaus.baader@sgcib.com

China
Wei Yao
 (852) 2166 5437
 wei.yao@sgcib.com

Michel Martinez
 (33) 1 4213 3421
 michel.martinez@sgcib.com

Omair Sharif
 (1) 212 278 48 29
 omair.sharif@sgcib.com

Japan
Takuji Aida
 (81) 3 5549 5187
 takuji.aida@sgcib.com

Korea
Suktae Oh
 (82) 2195 7430
 suktae.oh@sgcib.com

Yvan Mamalet
 (44) 20 7762 5665
 yvan.mamalet@sgcib.com

Latin America
Dev Ashish
 (91) 80 2802 4381
 dev.ashish@socgen.com

Kiyoko Katahira
 (81) 3 5549 5190
 kiyoko.katahira@sgcib.com

India
Kunal Kumar Kundu
 (91) 80 6716 8266
 kunal.kundu@sgcib.cz

United Kingdom
Brian Hilliard
 (44) 20 7676 7165
 brian.hilliard@sgcib.com

Ankur Shukla
 (91) 80 6731 4432
 ankur.shukla@sgcib.com

Arata Oto
 (81) 3 6777 8064
 arata.oto@sgcib.com

Inflation
Vaibhav Tandon
 (91) 80 6731 9449
 vaibhav.tandon@sgcib.com

SG CROSS ASSET RESEARCH - FIXED INCOME & FOREX GROUPS

Global Head of Research
Brigitte Richard-Hidden
 (33) 1 42 13 78 46
 brigitte.richard-hidden@sgcib.com

Head of Fixed Income & Forex Strategy
Vincent Chaigneau
 (44) 20 7676 7707
 vincent.chaigneau@sgcib.com

Fixed Income
Bruno Braizinha
 (1) 212 278 5296
 bruno.braizinha@sgcib.com

Jorge Garayo
 (44) 20 7676 7404
 jorge.garayo@sgcib.com

Head of US Rates Strategy
Subadra Rajappa
 (1) 212 278 5241
 subadra.rajappa@sgcib.com

Foreign Exchange
Jason Daw
 (65) 63267890
 jason.daw@sgcib.com

Head of Emerging Markets Strategy
Guy Stear
 (33) 1 41 13 63 99
 guy.stear@sgcib.com

Amit Agrawal
 (91) 80 6758 4096
 amit.agrawal@sgcib.com

Phoenix Kalen
 (44) 20 7676 7305
 phoenix.kalen@sgcib.com

Frances Cheung, CFA
 (852) 2166 5437
 frances.cheung@sgcib.com

Ciaran O'Hagan
 (33) 1 42 13 58 60
 ciaran.ohagan@sgcib.com

Jason Simpson
 (44) 20 7676 7580
 jason.simpson@sgcib.com

Alvin T. Tan
 (44) 20 7676 7971
 alvin-t.tan@sgcib.com

Jean-David Cirotteau
 (33) 1 42 13 72 52
 jean-david.cirotteau@sgcib.com

Shakeeb Hulikatti
 (91) 80 2802 4380
 shakeeb.hulikatti@sgcib.com

Marc-Henri Thoumin
 (44) 20 7676 7770
 marc-henri.thoumin@sgcib.com

Olivier Korber (Derivatives)
 (33) 1 42 13 32 88
 olivier.korber@sgcib.com

Cristina Costa
 (33) 1 58 98 51 71
 cristina.costa@sgcib.com

Adam Kurpiel
 (33) 1 42 13 63 42
 adam.kurpiel@sgcib.com

Régis Chatellier
 (44) 20 7676 7354
 regis.chatellier@sgcib.com

Jason Daw
 (65) 6326 7890
 jason.daw@sgcib.com

Frances Cheung, CFA
 (852) 2166 5437
 frances.cheung@sgcib.com

Disclaimer

The information herein is not intended to be an offer to buy or sell, or a solicitation of an offer to buy or sell any securities. All information and opinions have been obtained from or are based on sources believed to be reliable, but their completeness and accuracy are not guaranteed by Komerční banka, a.s., even though Komerční banka, a.s. believes them to be fair and not misleading or deceptive. The views of Komerční banka, a.s. reflected in this document may change without notice.

Komerční banka, a.s. and its affiliated companies may from time to time deal in, profit from the trading of, hold or act as market makers of securities, or act as advisers, brokers or bankers in relation to securities or derivatives thereof emitted by persons, firms or entities mentioned in this document.

Employees of Komerční banka, a.s. and its affiliated companies, or individuals connected to them including the authors of this report, may from time to time have a position in or be holding any of the investments or related derivatives mentioned in this document. Komerční banka, a.s. and its affiliated companies are under no obligation to provide any services to their clients on the basis of this document.

Komerční banka, a.s. does not accept any liability whatsoever arising from the use of the material or information contained herein beyond what is required by law. This research document is primarily intended for professional and qualified investors. Should a private customer obtain a copy of this report, they should not base their investment decisions solely on the basis of this document and should seek independent financial advice. The investors must make their own informed decisions regarding the appropriateness of their investments because the securities discussed in this report may not be suitable for all investors.

The performance attained by investment instruments in the past may not under any circumstance serve as an guarantee of future performance. The estimates of future performance are based on assumptions that may not be realized. Investment instruments and investments are connected with different investment risks, the value of any investment can rise and fall and there is no guarantee for the return of the initial invested amount. Investment instruments denominated in foreign currencies are also subject to fluctuations caused by changes in exchange rates, which can have both positive and negative influences particularly on the prices of the investment instrument and consequently on the investment return.

This publication is issued by Komerční banka, a.s. which is a bank/stockbroker according to the applicable legislation and thus regulated by the Czech National Bank. Komerční banka, a.s. applies various measures to prevent conflict of interests in the process of creating investment recommendations, such as the implementation of an appropriate internal separation including information barriers between different departments of Komerční banka, a.s. in compliance with the requirements imposed by applicable regulation. The employees of Komerční banka, a.s. proceed in accordance with the internal regulations governing conflict of interest.

The evaluation of employees creating investment recommendations is never by any means tied with the volume or profit of the trades with instruments mentioned in this document done by Komerční banka, a.s., or the trades of Komerční banka, a.s. with the issuers of such instruments. However, the evaluation of the authors of this document is linked to the profits of Komerční banka, a.s. which also partially include the results of trading with investment instruments.

The recommendations mentioned in this document are intended for the public and the document before its publication is not available to persons not involved in the creation of this document. As per our practice, the issuers usually do not receive a copy of research reports prior to their publication. Each author of this research report hereby states that (i) the views expressed in the research report accurately reflect his or her personal views about any and all of the securities or issuers at stake.

This document and its contents is not designed for persons with permanent residence or seat in the United States of America and to persons who are deemed as "U.S. persons", as defined in Regulation S under the US Securities Act of 1933, as amended.

Please refer to our website <http://www.trading.kb.cz> for more details.