CEE currencies weather storms in European debt crisis

BUCHAREST, Aug. 6 (Xinhua) -- This isn't a hot a summer for the CEE (Central and Eastern Europe) currencies, which managed to avoid the turmoil that is shaken the eurozone. But the picture is complex. While Polish zloty looks like a safe heaven for investors, the Hungarian forint is rather a speculative attraction, the Czech koruna is flat and rather boring, and Romania leu is spooky. The Polish zloty defies the European markets volatility, the Hungarian forint recoup its loses with a speed fueled by investor's hopes that a deal with International Monetary Fund (IMF) will finally be stamped in Autumn. Meanwhile the Czech koruna posted moderate growth and Romanian leu remains under pressure for some time, due to political turmoil. The worst performer in CEE, the Romanian leu has depreciated 2.7 percent in July amid deteriorating economy, fears of the Greek contagion and noisy political scene. Romania's leu was first seen by the financial markets as a fragile currency standing on a banking sector extensively linked with Greece, and then was hurt by uncertainties raised by internal political struggles. The leu fell to the lowest in all times, 4.6481 lei for one euro on Friday, as the political incertitudes intensified. Mugur Isarescu, the governor of the Romanian central bank, warned that the outlook of the economy is not promising, with a lower agricultural output due to the draught and a headwind in consumption. He mentioned in a surprise press conference in the very day in which he decided to keep monetary policy rate at 5.25 percent that the risk of deleveraging is intense, as there were sizeable capital outflows in recent months. He added that non-resident investors cut their holdings of government debt and some maturing bank debt was not refinanced. According to estimations of Romania's Commercial Bank, the outflow produced by non-resident's flee from their Romanian bonds holding was relatively small - worth 0.2 percent of GDP in the second quarter. "At the end of May, foreign investors held the equivalent of 2.6 billion euro in Romanian debt (lei and foreign currencies combined), representing 11.2 percent of the total. Local banks held two thirds of Romanian treasury paper (15.3 billion euro), with other local investors holding a fifth of the amount," noted Dan Bucsa, chief economist at Unicredit Tiriac Bank Romania. Euro area woes explained the scarce and volatile external financing and the weaker leu. "Recent political turmoil has probably worsened the situation," added Bucsa. The Romanian currency has turned from being one of the most stable currencies in the region to being the regional laggard, with a 7 percent depreciation year on year while zloty and forint are almost unchanged, said Vlad Muscalu, chief economist at ING Bank Romania. FORINT, THE FASTEST RECOUP The best performer of the moment is the Hungarian forint, which strengthened by 12 percent versus euro since the beginning of the year, and gained 3 percent in July jumping to 278.94 forints per euro. As most of the investors are betting on a deal with the IMF and the European Union which may happen in September-October, that could keep the forint in a strong position. The country's trade balance showed quite a comfortable surplus of 701million euro in May, which may supported the gains of the forint or, at least, put no pressure of depreciation. But the analysts noted that the forint appreciation is happening on low trading volumes, meaning that markets are still thoughtful. Meanwhile the Hungarian central bank is keeping its key interest rate intact at 7 percent, the highest level in CEE, and that exercise may convince speculative investors to bet on forint. However, "sentiment on the Eurozone will be the decisive driver for the forint markets," said Raiffeisen Bank analyst Stephan Czaba Imre in a note to investors, warning that "the IMF negotiations will be bumpier than the consensus currently thinks." A BIT OF A SAFE HEAVEN The Polish zloty gained almost 9 percent in the first seven month of the year, fuelled by a resilient economy and deeper money markets than its peers from CEE region. In July, the zloty continued its appreciation, gaining 3.38 percent versus euro, climbing from 4.2488 to 4.1050 zloty per euro. "To some extent the Polish zloty was a little bit of a safe heaven in the European environment and this is somehow justified given the economy fundamentals," said Lars Christensen, Danske Bank's chief analyst for EMEA to Xinhua. The Poland's public finance is in good shape, with decreasing budget deficit and finance needs secured by third quarter of 2012, and the solid economic growth is still the highest in the European Union. However there are signals that the Polish economy is slowing and the probability of a deterioration in economic activity in the second half of the year is higher, warned Dorota Strauch, analyst at Raiffeisen Bank, in a report. "The slowdown of the economy is, however, inevitable, due to the emerging recession in the Eurozone and weakening domestic demand. We keep our forecast of 2.6 percent GDP growth for 2012," estimated the Erste Group research team in a note to investors. Meanwhile the Polish sovereign bonds are in high demand and that is fuelling the zloty. CHEAP MONEY, LOW YIELDS The Czech koruna enjoyed a moderate appreciation, almost entirely due to the European Central Bank chief Mario Draghi's supportive actions on behalf of eurozone. The Czech Republic is delivering cheap money for its economy and that is barely an incentive for spectacular appreciation of the currency. The koruna gained 1.6 percent in July to 25.258 koruna per euro from 25.640. The Czech central bank (CNB) is keeping its key policy rate unchanged at 0.50 percent and analysts expect that is moving towards an exercise of quantitative easing. There will be weak support, if any, from the real economy for Czech's currency. "It looks more like the Czech economy is falling deeper into recession. Second-quarter GDP is likely to show that the economy fell into a deeper recession than in the first quarter of 2012. We expect the Czech economy to contract by 1.3 percent year on year in 2012," noted Christensen.