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Macro Hive Pro: EM Focus – CEEMEA C/A and FX Outlook

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Summary

- CEE C/A adjustment is set to stall or even reverse in 2024 as domestic demand picks up and the earlier boost from falling energy prices ends.
- Turkey's C/A correction will continue with a significantly tighter monetary policy stance and a broadly neutral fiscal stance.
- For South Africa, large investment needs will offset a boost to exports from any rebound in Chinese export demand.

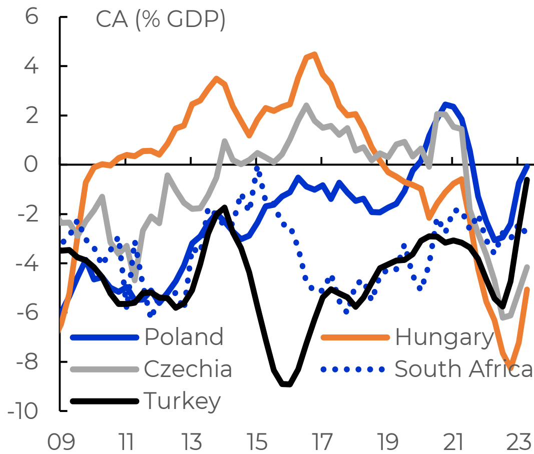
Market Implications

- With Poland's new government, now in place we remain bullish PLN short-term.
- But rising fiscal risks leave us increasingly bearish medium-term.
- CZK weakness should accelerate as rate cuts pick up pace. Stay long EUR/CZK.
- South Africa's general election and the prospects for US rate cuts leaves a potentially volatile H1 for the rand.
- High interest rates and a more orthodox policy stance leaves us bullish TRY.

CEEMEA C/As to Diverge in 2024

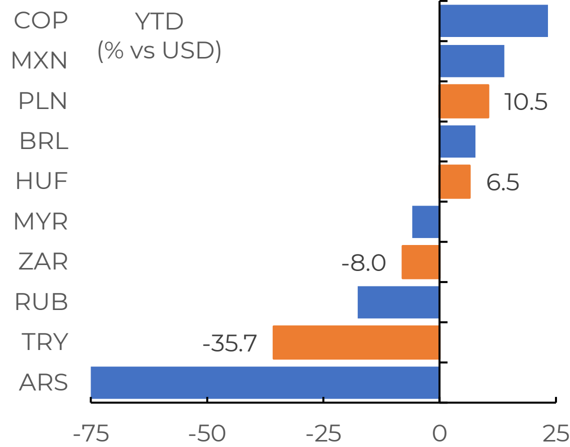
Current accounts adjusted sharply in CEE and Turkey in 2023. South Africa's deficit also came in from the Q2 wides (Chart 1). But with the big correction in energy prices largely done and domestic demand set to pick up in parts of the region, 2024 is likely to see C/A adjustment stall or possibly reverse in CEE. The outperformance of HUF and PLN in 2023 is therefore unlikely to be repeated (Chart 2). For TRY, high interest rates and a more orthodox policy mix should mean a better performance in 2024, albeit with uncertainty related to the March local election.

Chart 1: CEEMEA Region Saw Sharp C/A Adjustment in 2023



Source: Macro Hive, Macrobond

Chart 2: CEEMEA Currencies Were Amongst the Best and Worst Performers



Source: Macro Hive, Macrobond

Energy prices, demand recovery will curb further C/A improvement. CE3 plus Turkey benefitted from the drop in oil (around 18%) and gas (around 70%) prices versus the 2022 highs. Hungary's energy deficit peaked at 10% of GDP in 2022 but is now closer to 6.2% of GDP (Chart 3). All four countries also benefitted from import compression due to weakness in domestic demand. For Turkey, this was more a H2 story as the new economic team increasingly tightened policy from the very expansionary stance ahead of the May election.

Weak domestic demand was also a factor in South Africa's improving C/A in Q3. But as an energy exporter, and one heavily reliant on China, South African exports suffered from sluggish end market demand, ToT weakness, and exacerbating logistical constraints.

Poland's economy already rebounding. Poland's recovery is already underway with H2 2023 seeing a rebound in retail sales and IP and Q3 growth at a strong 1.4% QoQ. Hungary, and particularly Czechia, have yet to see the same rebound with Q3 GDP at 0.8% and -0.5%, respectively, and high frequency data also confirming ongoing weakness. But momentum is nevertheless expected to improve in 2024, with real wage growth increasingly positive and lower interest rates triggering an improvement in the weak credit dynamics.

Stronger domestic demand will see import growth improve from the current lows. Meanwhile, the levelling off in energy prices will mean the 2023 benefit from lower energy prices is largely over. For CE3 and Turkey, sluggish growth in Europe will mean export growth remains constrained.

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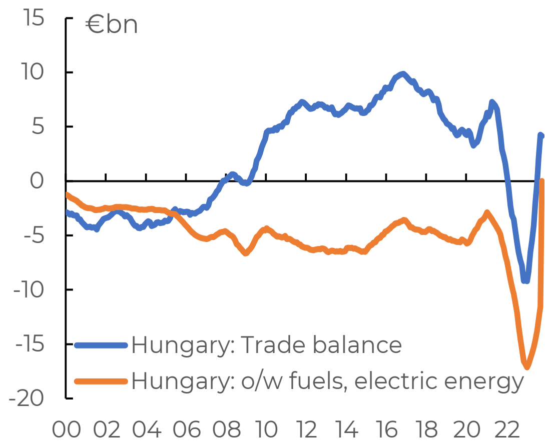
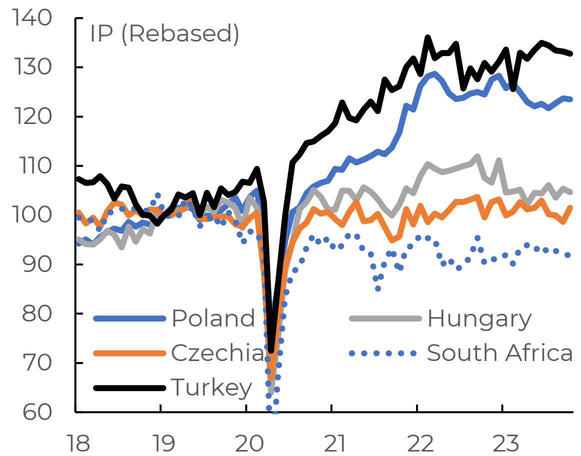
Chart 3: Lower Energy Prices Drove Trade, C/A Correction in Hungary



Source: Macro Hive, Macrobond

Chart 4: Post-Pandemic Recovery Has Been Mixed Across the Region

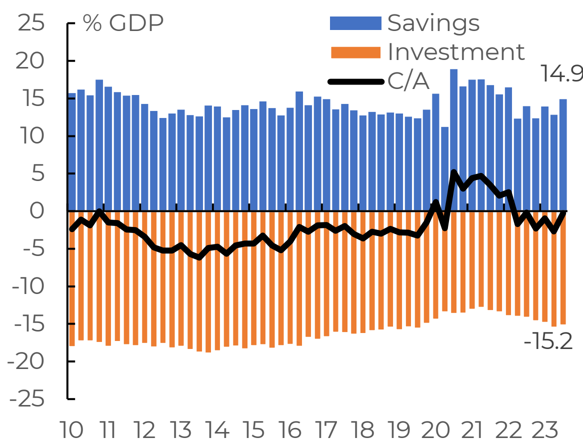


Source: Macro Hive, Macrobond

South Africa's investment needs will limit C/A adjustment. South African exports could pick up should we see a meaningful improvement in Chinese growth. But the country's ongoing investment needs will limit the extent of any C/A improvement. Investment/GDP in South Africa is now lower than the long-term average, and capex needs are high given the deep energy and logistics problems related to inefficiencies at Eskom and Transnet (Chart 5). External savings will therefore be needed going forward to finance South Africa's savings-investment gap.

For CEE, the savings-investment dynamics that stand out are in Czechia. The 2023 C/A improvement was driven by a combination of rising savings and a modest decline in investment. As interest rates start to decline and consumer confidence improves, the savings rates should drop from the recent highs, limiting further C/A improvement.

Chart 5: South Africa's Investment/GDP Ratio Lower Than Historical Average



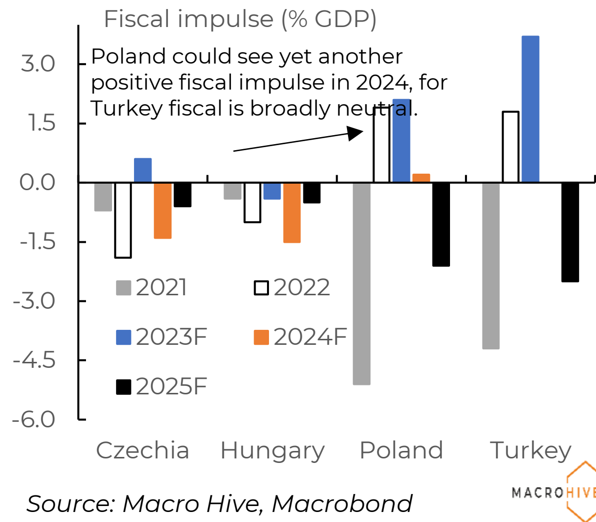
Source: Macro Hive, Macrobond

Public versus private and the fiscal outlook. Fiscal dynamics will also determine the C/A adjustment in 2024. Poland again stands out as the country where the 2023 C/A correction could reverse. The country's new KO-led government has yet to revise the 2024

budget and we do not yet have full clarity on which pre-election spending promises will be delivered. But with expectations for the 2024 fiscal deficit increasingly approaching 6% of GDP, Poland could see yet another positive fiscal impulse next year.

For Turkey, reconstruction costs from the February 2023 earthquake and potential spending ahead of the local elections will mean the fiscal deficit remains large at around 6% of GDP. But fiscal policy is unlikely to be more expansionary than in 2023, leaving the fiscal stance broadly neutral.

Chart 6: Turkey's Fiscal Stance Neutral in 2024, Poland's Still Expansionary



Source: Macro Hive, Macrobond

2024 CEEMEA FX Outlook

PLN – Still bullish short-term but rising fiscal risks to end PLN strength. We have been bullish on the zloty in recent months due to the change of government and related EU inflows and improved investment outlook. With the new government just one week old, we think zloty strength has a bit further to run. But with fiscal risks coming to the fore, continued PLN strength past Q1 is unlikely.

Hungary – Remaining neutral HUF on mixed dynamics. Rising export capacity from earlier EV investment will support exports in 2024. This should offset some of the import rebound from improved domestic demand. But with the benefit from lower energy prices over and increasingly lower interest rates eroding the once-high carry, we retain our neutral stance for 2024.

Czechia – CZK weakness to accelerate in 2024 as easing gathers pace. A slow but steady improvement in growth from the protracted weakness over recent quarters should see import growth pick up. And combined with the decline in savings from lower rates, the C/A improvement should start to reverse. Significant reliance on Germany will also continue to weigh on exports. A weaker C/A position and accelerated rate cuts as inflation drop towards target in Q1 points to continued CZK weakness.

South Africa – A volatile H1 ahead for ZAR. Capital account dynamics will continue to dominate any C/A deficit. And with market expectations for the US Federal Reserve to

start cutting rates from March, the rand could benefit from improved risk sentiment. But with the general election due in April / May ZAR could be in for a volatile H1.

Turkey – Remaining bullish TRY. A significantly tighter monetary policy stance in 2024 and a broadly neutral fiscal stance should see Turkey's C/A correction continue. Interest rates are set to remain high and foreign inflows are trickling in. Underperformance of TRY should come to an end. And while gains are likely to be modest with still-high inflation and risks around the local elections, we retain our bullish stance.

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