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CFA Society Forecasting Dinner 2013 Survey

Final Survey Report
February 2013

Dear readers,

We hereby present you with the final report from our latest survey, which was carried out on the occasion of the CFA Society Forecasting Dinner 2013. As is the case each year, the dinner is being organized by the CFA Society Czech Republic. We again turned to Donath Business & Media and ppm factum research to gauge the views of key circles of professionals to current issues facing the Czech economy.

Our focus this year was directed toward assessment of fiscal and monetary policy, expectations regarding construction of the Temelín nuclear power plant, and the second pillar of pension reform. We also sought to views on the risks posed by unethical behavior on the domestic financial markets.

We firmly believe that the following pages will offer you some inspiring food for thought.

Marek Jindra, CFA
President
CFA Society Czech Republic

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About the survey

The survey has been carried out on the occasion of the CFA Society Forecasting Dinner 2013, held as the 11th annual meeting of the CFA Society Czech Republic, an association of certified financial analysts. The event brings together leading local and foreign economic experts to discuss the economic forecasts for the coming year, under the auspices of the governor of the Czech National Bank, Miroslav Singer, who will also be in attendance.

The survey was conducted for the CFA Society Czech Republic online by Donath Business & Media and ppm factum research between 23 January and 5 February 2013 and aims to reveal the current issues facing the Czech economy, as perceived by economists and financial professionals.

The following people were invited to participate in the survey:

- Members of the CFA Society Czech Republic and CFA Program candidates;
- Leading figures from the Czech business and financial sector;
- Readers of The Fleet Sheet's Final Word electronic bulletin;
- Journalists.

Questions related to:

- Assessment of fiscal and monetary policy;
- Expectations for the Temelín enlargement and implementation of the second pillar of pension reform;
- Levels of unethical behavior on domestic financial markets, and yields generated by various types of assets.

Out of 8,202 people who were addressed, 1,796 participated in the survey (i.e. a 22 % response rate). The views of the respondents on individual questions are detailed in the next part of the report.

Key findings

The government's fiscal policy does not support economic growth. However, the decision to consolidate public finances was good. Although 82% of the respondents do not regard fiscal policy as growth-enhancing, 80% believe it was right to push through the deficit-reduction program.

The Czech National Bank's monetary policy creates an opportunity for economic growth, though its leaders' appeals for support for household expenditures are far from convincing. Most respondents (61%) believe the CNB's monetary policy promotes economic growth. A great majority of the respondents (81%) also think the CNB's appeals will not bring about any change in the consumer behavior of the population. The respondents do not have a common point of view regarding Czech membership in the European banking union.

The construction of Temelín could boost the economy. However, the government should not guarantee the price of energy. Most respondents (59%) believe the construction of the Temelín nuclear power plant could help boost economic growth in the Czech Republic. However, experts strongly believe (69%) that the government should not guarantee the price of energy to the operator of Temelín. Almost twice as many respondents (25%) forecast that the Škoda JS/Rosatom consortium will win the tender over Westinghouse (14%).

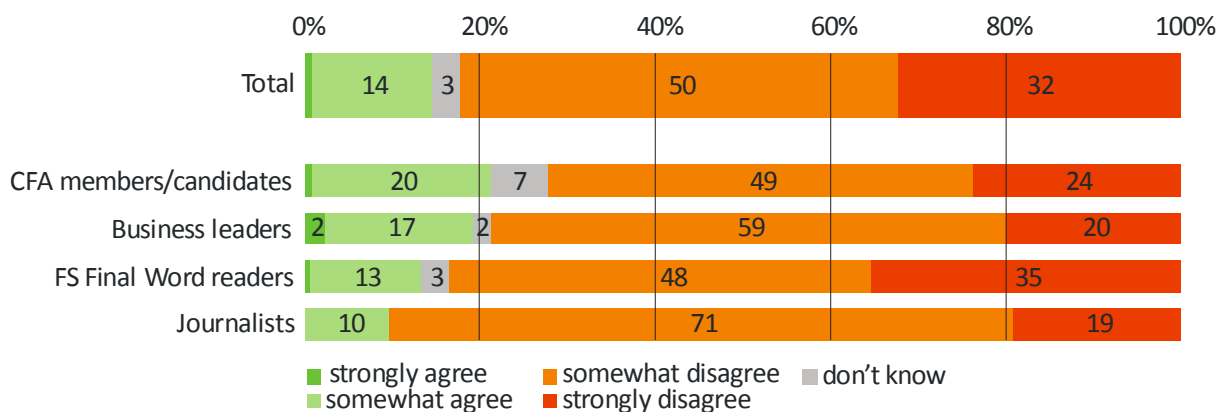
The second pillar of pension reform is regarded with mistrust. Only 8% of the respondents expect the next government will keep the second pillar unchanged. Most (57%) believe that fewer than 200,000 people will register for the new system in the first half of 2013. Sixty-three percent of the respondents think the current pension reform lacks the potential to stabilize public finances in the long term.

Market fraud is believed to pose the greatest risk of unethical behavior on Czech financial markets. The assets with the best yields should be precious metals and commodities.

Growth or restraint

Fiscal policy is always subject to political differences, especially in times of economic difficulties. Czech gross domestic product dropped 1.1% in 2012. We are suffering from the longest recession since 1997, when the economy also fell for four successive calendar quarters. In this unfavorable economic situation, the government has decided to continue its endeavor to cut the public deficit. Is this a wise policy?

Does the government's fiscal policy support economic growth?

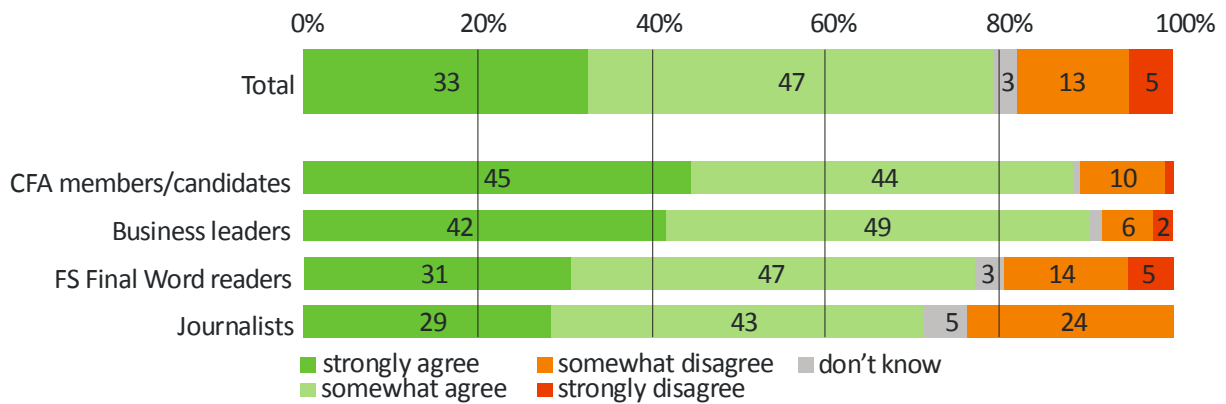


Four-fifths of the respondents stated that the government's fiscal policy does not support economic growth. The most critical in this assessment are readers of the Final Word bulletin and journalists. On the other hand, leading managers and CFA members are the least strict. The older the respondents, the more likely they are to strongly disagree that the government's fiscal policy supports economic growth.

In circumstances when Finance Minister Miroslav Kalousek has claimed we must not keep piling up debts in order to support economic growth and that unpopular measures are necessary, this is only stating the facts. Despite this, 15% of the respondents believe the current fiscal policy promotes growth, probably in the midterm or long-term view.

We may expect the economic situation to turn positive from the second quarter of 2013 at the earliest. Even so, the year 2013 will see continued stagnation of the Czech economy. The only positive factor is exports, which have grown 4.3% in 2012.

Was it a good idea for the government to push through a deficit-reduction program last year?



Although 82% of the respondents do not regard fiscal policy as growth-enhancing, as implied from the previous question, 80% believe it was right to push through the deficit-reduction program.

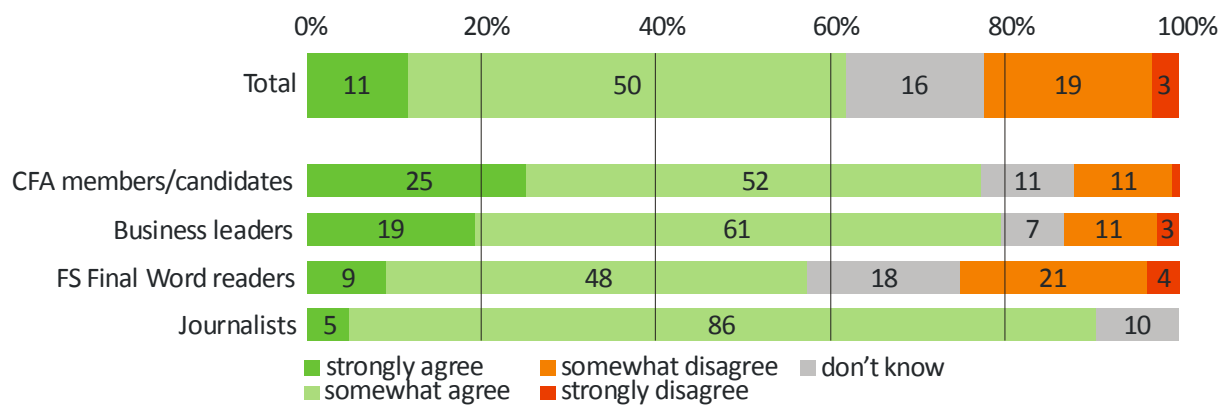
CFA members and candidates and leading managers are the most convinced that this was a good idea, much less so readers of the *Final Word* bulletin and journalists.

The view of most respondents is similar to the opinion of the vice-president of the European Commission, Olli Rehn, who pointed out to ECOFIN ministers in his letter dated 13 February 2013 that the stability culture embodied in Europe's reinforced economic governance does not stand in the way of sound, long-term growth. Rehn, a member of the European Commission responsible for economic and monetary affairs and the euro, maintains that consistent and carefully calibrated fiscal consolidation remains necessary in Europe and creates the conditions for sustainable growth for years to come.

The Czech National Bank and the economic recession

Respondents commented on the CNB's monetary policy and its calls for expanding domestic demand. We might mention that the CNB's mandate is to maintain price stability, oversee the stability of the financial system, ensure smooth circulation of money and smooth payments, and support the development of the Czech financial markets. Promotion of economic growth is not the principal objective of an independent central bank. Monetary policy is a powerful but not all-powerful instrument. Cutting rates in a time of crisis is a necessary but not sufficient condition for the recovery of economic growth. While most respondents (61%) appreciate maintaining price stability and low inflation as the CNB's continuous and valuable contribution to developing the potential for economic growth, only 12% of the respondents believe its leaders' calls for an increase in household expenditures can lead to any change in the consumer behavior of the population.

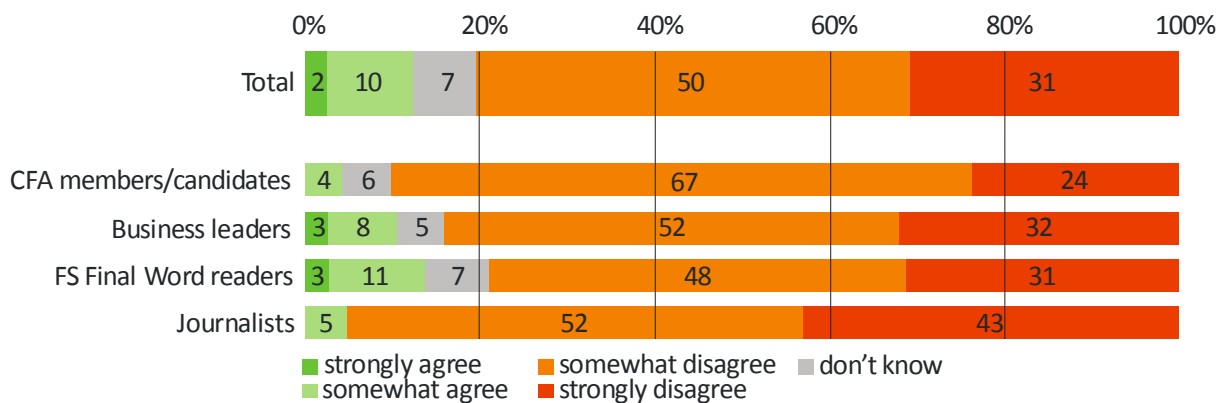
Is the CNB's monetary policy aimed at promoting economic growth?



Three-fifths of the respondents believe the CNB's monetary policy is aimed at promoting economic growth. However, one-fourth of the professional public are afraid the CNB's current monetary policy will not lead to economic growth.

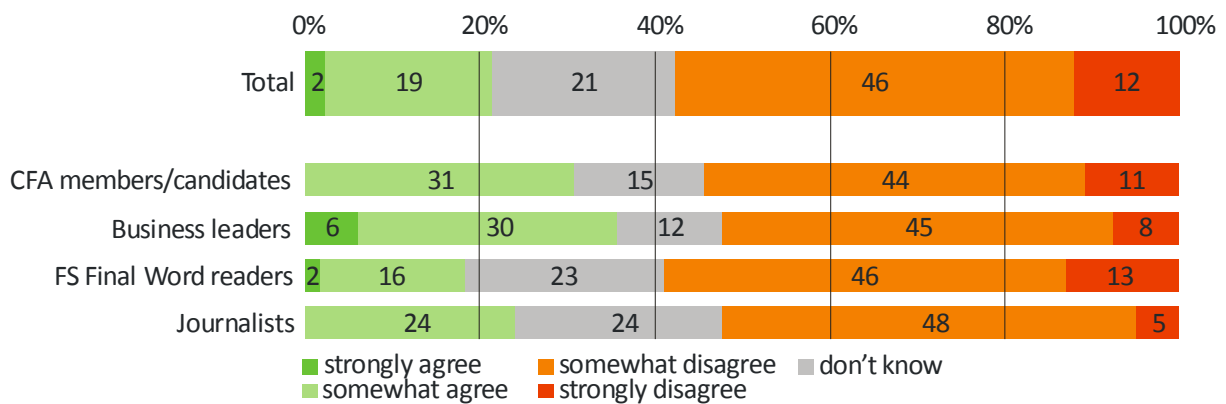
CFA members and candidates and the leading managers have a stronger belief that the CNB's monetary policy is aimed at promoting economic growth. Journalists are fairly optimistic regarding the CNB's activities in this area, although they express their views more reservedly – they "somewhat agree". The older the respondents, the less strongly they agree that the CNB's monetary policy is aimed at promoting economic growth.

Can the CNB's appeal for greater household consumption lead to a change in the behavior of the Czech population?



Words might be powerful, but this does not seem to apply when the leader of the central bank invites households to spend. Four-fifths of the respondents do not expect the CNB's appeal to affect the consumer behavior of the population. Journalists and CFA members and candidates have the least confidence in this; Final Word readers and leading managers are slightly more optimistic but still quite skeptical.

Are Czech banks effective in helping Czech companies succeed on foreign markets?

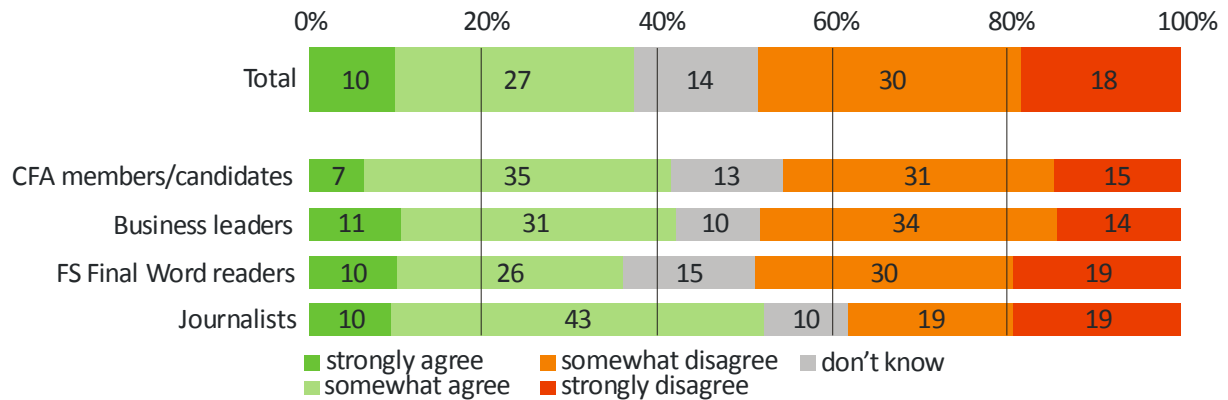


Foreign demand for Czech goods and services to a great extent determines the chances for an economic recovery in the Czech Republic. Success on foreign markets is not only dependent on having companies that are able to stand the test of international competition, but also on the support by domestic banks.

Fifty-eight percent of our respondents believe that Czech banks are not effective in helping Czech companies succeed on foreign markets. Only one in five experts has confidence that banks are capable of effectively helping in this respect. Interestingly, one-fifth of the experts had no answer to this question or did not wish to give one.

These results likely reflect the fact that the banks active in the Czech Republic have not been particularly effective so far in helping Czech companies (especially small and medium-sized businesses) on foreign markets, particularly with respect to the 12 priority countries as defined by the Czech Export Strategy passed by the government last year. This group of countries, including some of the "lost" markets, comprises Brazil, China, India, Iraq, Kazakhstan, Mexico, Russia, Serbia, Turkey, Ukraine, the United States and Vietnam.

Is the Czech government correct in arguing that membership in the European banking union represents a danger for the Czech Republic?



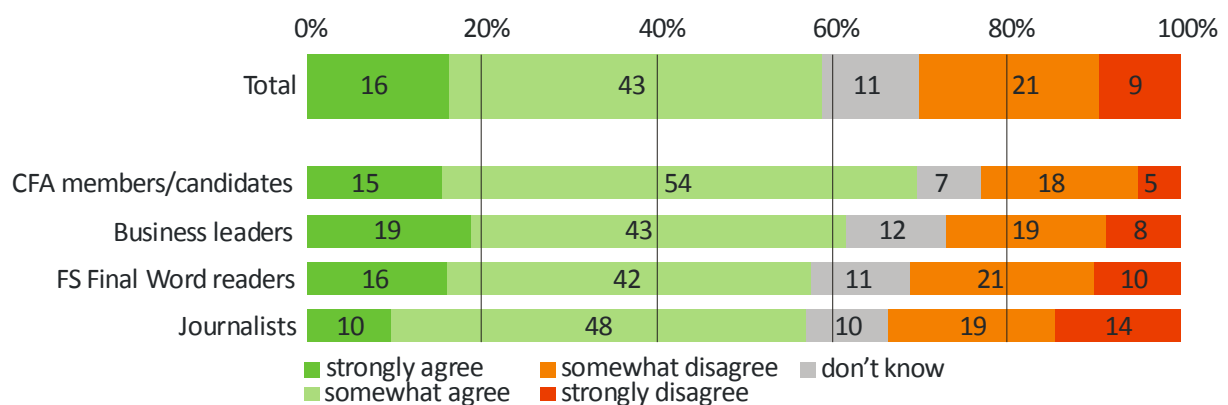
In response to the financial crisis, the EU has designed a project to establish a banking union that would introduce common deposit insurance, common supervision and a rescue fund. The banking union should be the first step toward further economic and monetary integration. The membership in the banking union is mandatory for all eurozone countries and voluntary for all other EU member states. The Czech Republic has not joined the banking union so far. At the EU summit in December 2012, the Czech Republic received guarantees that the system of common EU supervision of banks would not jeopardize the supervisory powers of the Czech National Bank or the stability of the Czech banking sector.

Forty-eight percent of the respondents disagree with the government's argument that Czech membership in the banking union represents a danger. However, the views are relatively balanced, as 37% of experts agree with the government and believe Czech membership in a European banking union poses a danger. This opinion is most frequently expressed by respondents older than 55 (59%). It reflects their concern that the system of common deposit insurance and the common framework for winding up failed banks would cause Czech banks to build up reserves and thus reduce the volume of disposable funds. As also pointed out by the CNB's leaders, there is the added danger of foreign parent companies turning their Czech subsidiaries into "branches" that would thus be no longer under the supervision of the CNB.

What to expect from the enlargement of Temelín?

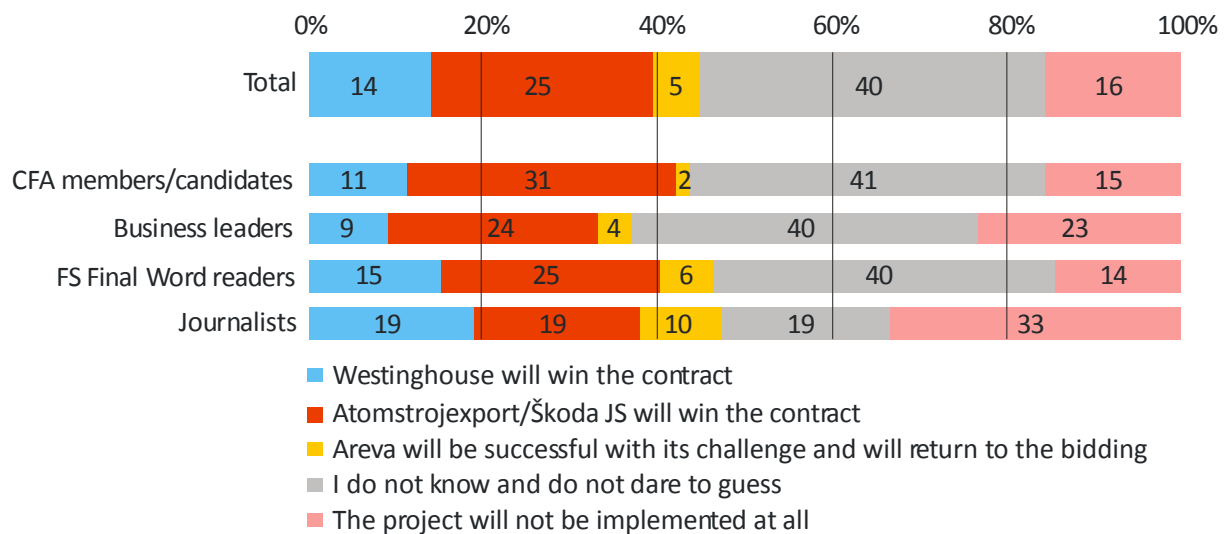
The construction of two new units at the Temelín nuclear power plant is the biggest procurement tender in the history of the Czech Republic. There is much speculation about the recoverability of this investment and the related government guarantee. We asked our respondents about the expected outcome of the tender, the guarantee for the price of electricity and the economic impact of the whole project.

ČEZ is preparing an investment into the construction of two nuclear blocks at Temelín. Can this project help the Czech Republic boost its economic growth?



ČEZ is preparing an investment of an estimated CZK 150-200 billion into the construction of two nuclear units at Temelín. All the individual bidders for the contract have been trying for some time to prevail on the public that their offer opens up a unique opportunity for Czech industry. This appeal seems to have been successful. Fifty-nine percent of the respondents believe the enlargement of Temelín can boost economic growth in the Czech Republic. CFA members and candidates are fairly optimistic. Journalists are slightly skeptical. Most supporters of the construction at Temelín are 55 and older (69%); these respondents believe this move can boost economic growth in the Czech Republic. Thirty percent of the professional public does not think this project can revive the economy.

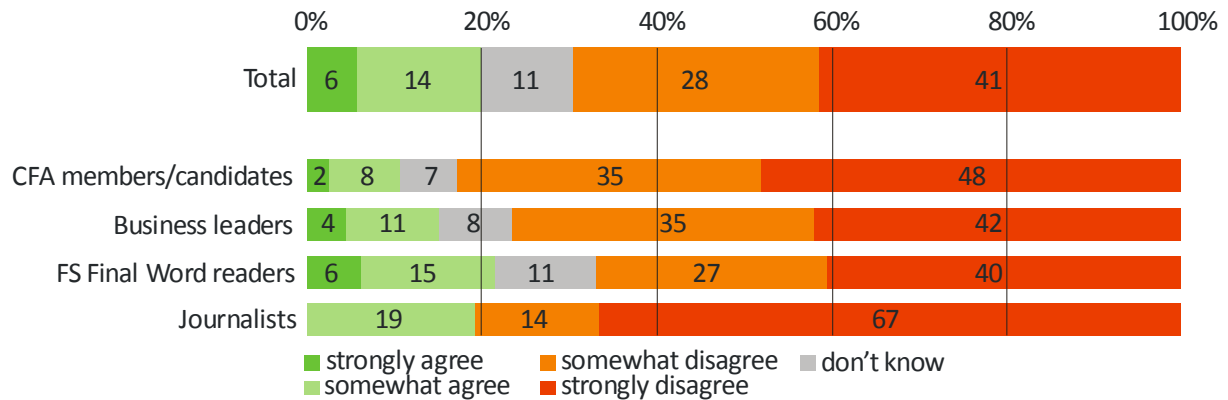
What outcome does the professional public expect for the Temelín tender?



Most respondents seem to pay close attention to the complicated situation surrounding the tender, which became even more intense when Areva was disqualified in October 2012. Areva's complaint was dealt with by the Office for the Protection of Competition. On 25 February it issued first-instance verdict under which by disqualifying Areva from the tender process, ČEZ did not breach the public procurement law. The United States supports the bid by Westinghouse, owned by Toshiba of Japan. Russia is lobbying for the Škoda JS – Rosatom consortium. ČEZ stated that the pre-assessment of bids shall be completed by the end of February and that the winner shall be announced in September.

Two-fifths of the respondents do not dare to guess the outcome of the Temelín tender. One in seven believes the project will not be implemented at all; this opinion is most often expressed by journalists and leading managers. The professional public is more of the opinion that Atomstrojexport / Škoda JS will win the tender (25%). Fourteen percent think Westinghouse will be the winner; however, the older the respondents, the less they believe that Westinghouse will win.

Should the Czech government provide an electricity-price guarantee for the operator of Temelín?



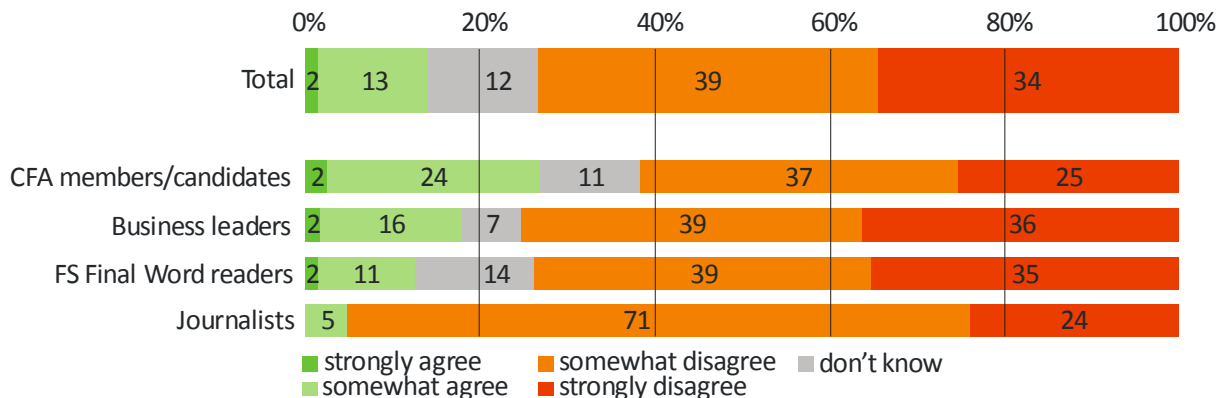
The professional public strongly believes the government should not guarantee the price of electricity to the operator of Temelín (69%). Two-fifths of the respondents "strongly disagree" with a price guarantee. The guarantee is firmly opposed by journalists, CFA members and candidates as well as respondents between 35 and 44 years of age (79%). Only one-fifth of the respondents are in favor of the price guarantee. There are more supporters of the guaranteed price among Final Word readers and respondents who are 55 and older (27%).

The current views of most respondents were undoubtedly affected by the affair concerning the guaranteed price of electricity produced by solar power plants. Moreover, it would not be easy to defend a government guarantee for the price of the electricity generated in Temelín before the European Commission.

Pension reform

On January 1, pension reform moved to the next phase. People over the age of 35 now need to make a decision by the end of June about whether to register for the second pillar managed by private pension funds. We asked what macroeconomic impact this reform measure might have and how much interest the second pillar will attract.

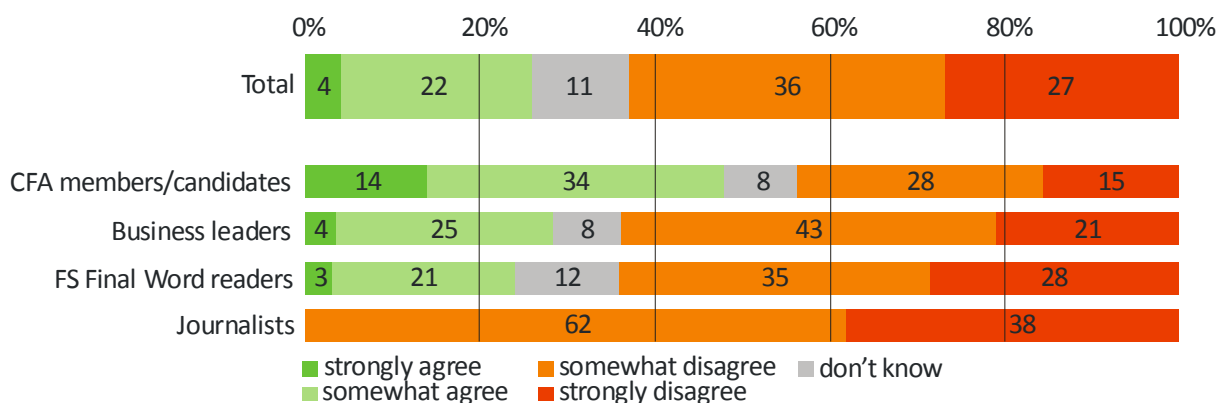
Will pension reform help promote economic growth?



Most financial analysts, leading local and foreign economic experts, and top managers are convinced that the current pension reform lacks the potential to boost economic growth (73%). This opinion is even stronger among journalists.

The professional public has little trust in the capability of pension reform to boost economic growth (15%). Slightly more optimism was expressed by CFA members and candidates (26%).

Will pension reform help stabilize public finances in the long term?

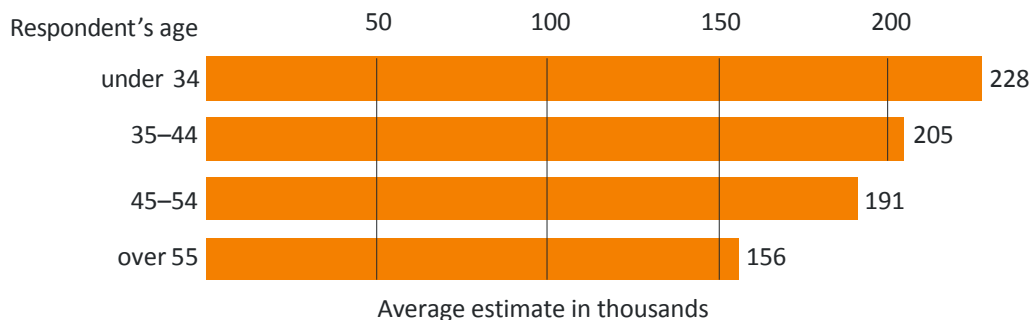
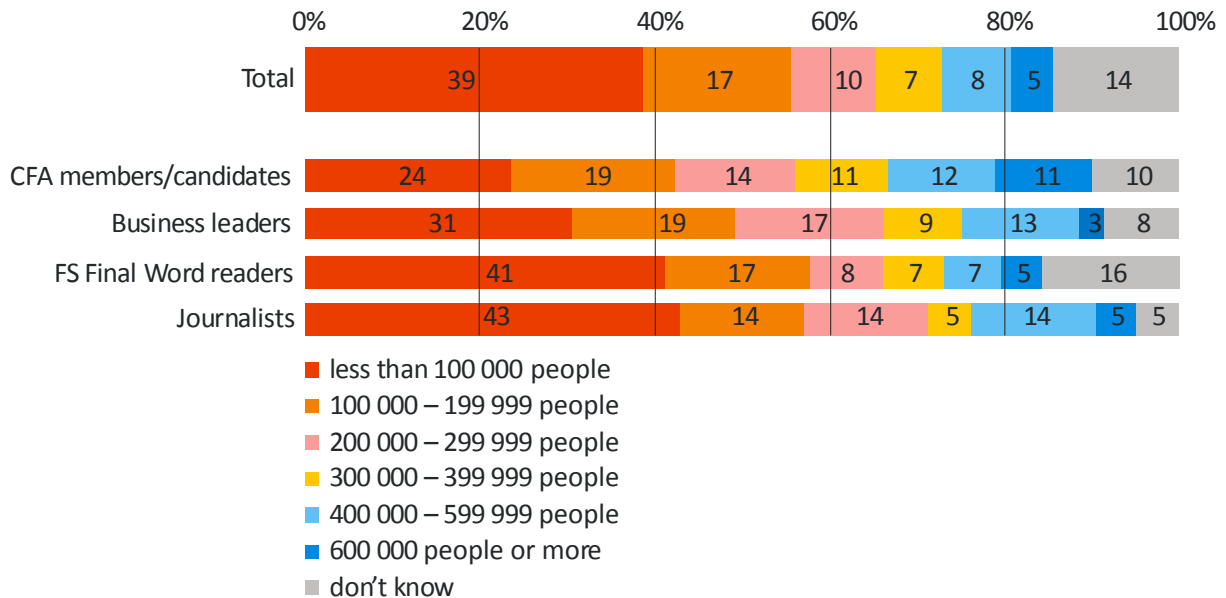


Most respondents believe the current pension reform lacks the potential to stabilize public finances in the long term (63%). This opinion is especially strong among the journalists.

One-fourth of the professional public regards pension reform as a factor that may help stabilize public finances in the long term. This opinion was given most often by CFA members and candidates and least often by Final Word readers. The older the respondents, the less they believe pension reform can stabilize public finances.

It remains a fact that the number of people who are economically active and contribute to the pensions of current pensioners is declining. The pension account has been in the red for four years, and last year's deficit was CZK 49.4 billion. As of today, the ratio is one pensioner to 1.8 people who are economically active and pay social security contributions. Unless the system is adjusted, this will be about 1.2 in 2050.

How many people will register for the second pillar in the first period (i.e. by 30 June 2013)?

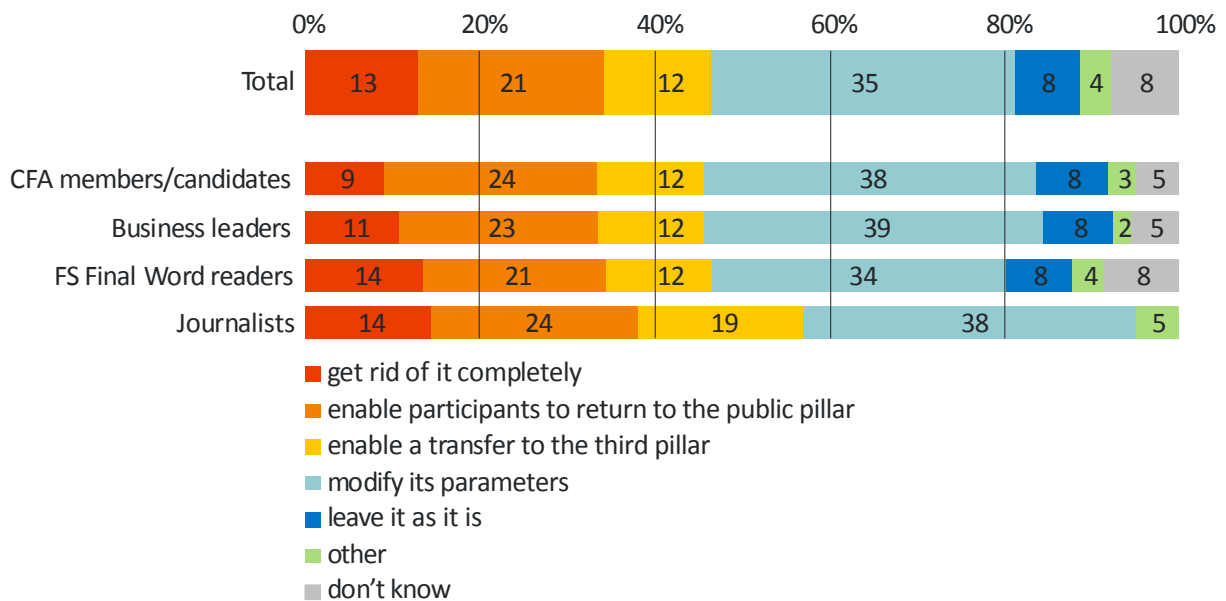


By the end of the first half of 2013, everyone who is of working age may register for the second pillar. After 30 June 2013, when the first period is complete, only people up to 35 will be allowed to join. There are about 1.3 million people over the age of 35 in the Czech Republic who must decide by the end of June 2013. The decision is irreversible; once registered, one may not leave. Only 7,300 people registered for the second pillar as of mid-February. However, the Association of Pension Funds of the Czech Republic believes this number will grow to half a million by the end of the first half of this year.

The average estimate of the number of people who will join the second pillar by 30 June 2013 is 193,000 (i.e. nearly 15% of people who are to decide by that time). Two-fifths of the professional public assumes it will be fewer than 100,000 people. Fifty-six percent of the respondents expect it will be fewer than 200,000.

CFA members and candidates estimate a higher number of participants, 277,000 people on average. Final Word readers are less optimistic; they expect 183,000 people to join on average. The older the respondents, the more significant the drop in the number of persons they expect to register for the second pillar by 30 June 2013.

How will the next government deal with the second pillar?



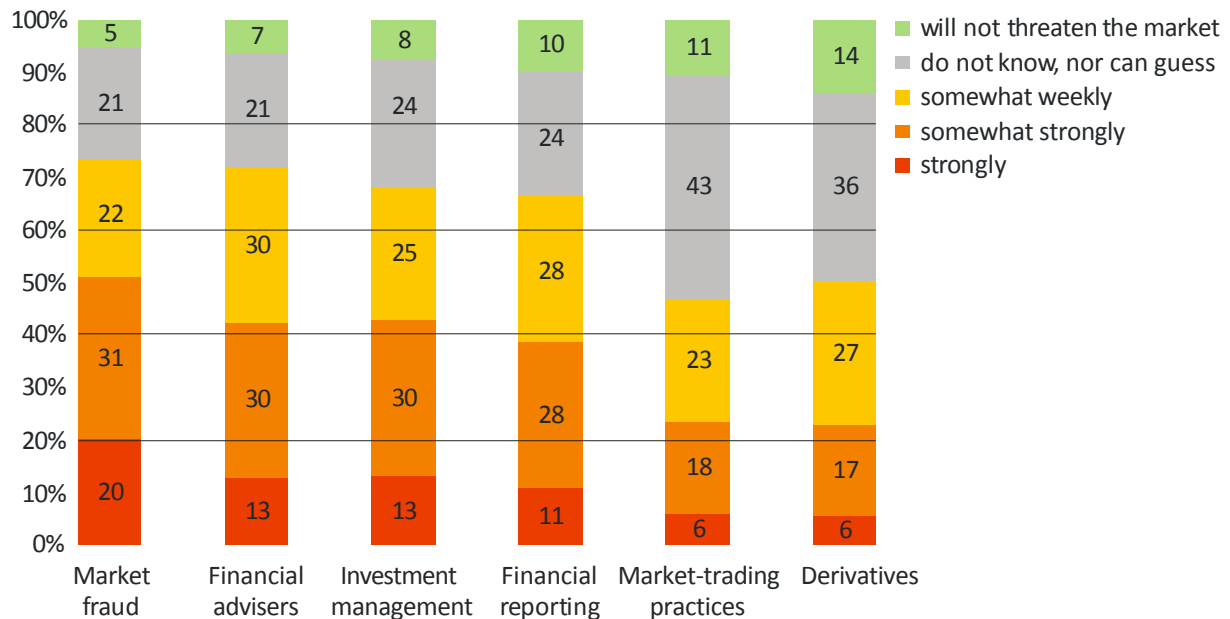
Responses to this question clearly reflect the fact that in Hungary, Poland and Slovakia a similar system was subject to major changes implemented by post-reform governments. Also, the ČSSD has tried to delay pension reform, and although it has not been successful, it is determined to stop it as soon as it gets the opportunity.

One-third of the respondents believe the next government will effectively stop the second pillar. One-half of the professional public expects that, after making certain changes, the government will continue to motivate people to invest in their pension savings. Eight percent of experts assume the next government will leave the second pillar as it is. There are no great differences among individual groups of respondents.

Dangers to the Czech financial markets and asset yield

The following two questions, which concern the risks to financial markets and the yield of various types of assets, were borrowed from the annual survey conducted by the CFA Institute, which aims to assess investor sentiment on the world markets. We do not have the survey results from previous years in order to evaluate the outcome; however, we will have them available next year.

To what extent will the following types of unethical behavior endanger Czech financial markets in 2013?



The respondents assessed the risk of unethical behavior in the following areas:

- Market fraud: insider trading or other abuses of confidential information
- Financial advisers: improper practices in the sale of financial products
- Investment management: inappropriate compensation structures favoring investment managers at the expense of clients
- Financial reporting: lapses in the honesty and integrity of financial reporting in general
- Market-trading practices: use of such things as dark pools and high-frequency trading
- Derivatives: improper use or disclosure of financial derivatives by financial firms

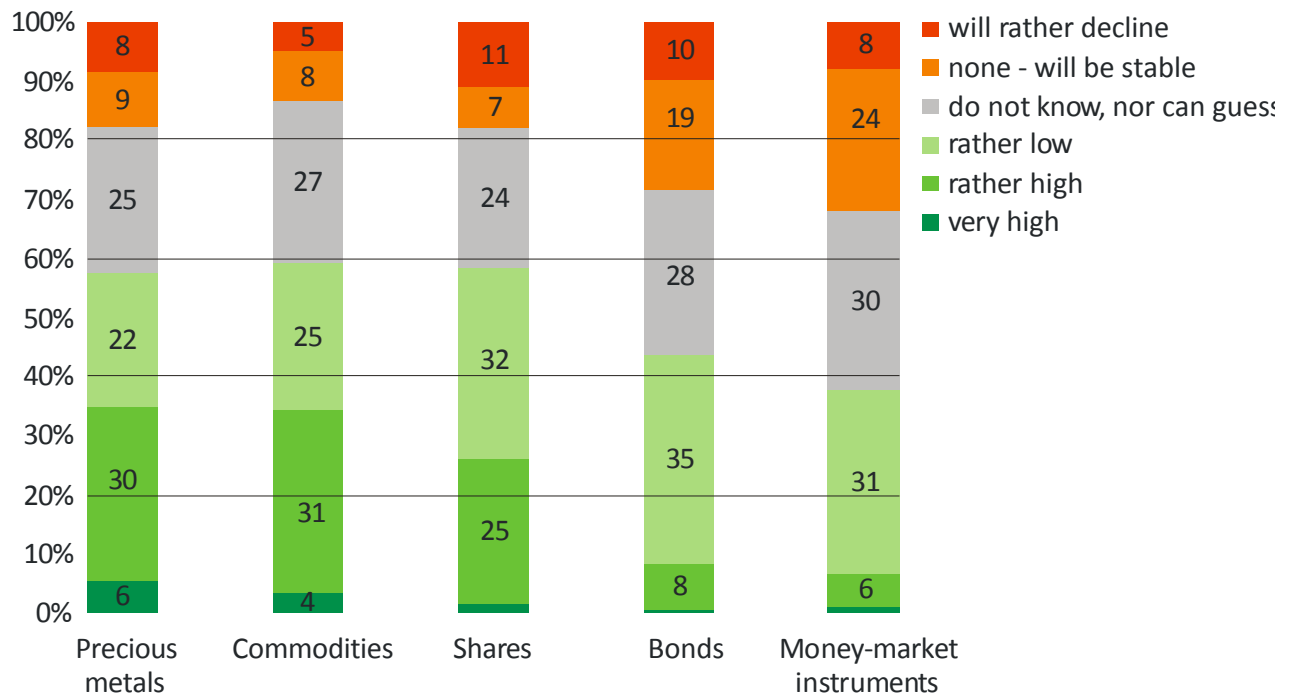
The respondents have concluded that in 2013 Czech financial markets will be most endangered by market fraud.

The risk of improper practices by financial advisers and the risk of inappropriate compensation structures favoring investment managers at the expense of clients follow by a narrow margin. Next are lapses in the honesty and integrity of financial reporting, again by a small margin. CFA members and candidates and leading managers are more optimistic than the respondents as a whole regarding all types of risks except for the danger posed by financial advisers. About twice as many of them (compared with the respondents as a whole) believe unethical behavior in these areas will not endanger the Czech financial markets at all.

Scandals have lately erupted even on well-established financial markets. Some banks have cheated when fixing the LIBOR London reference rate; others violated financial sanctions against Iran, and yet others took part in money-laundering in Mexico. This unethical behaviour was committed by major banks, which

strengthened the position of those politicians and regulators who believe some banks have not only become too big but also too complicated to regulate.

What yield will be generated by the following types of assets in 2013?



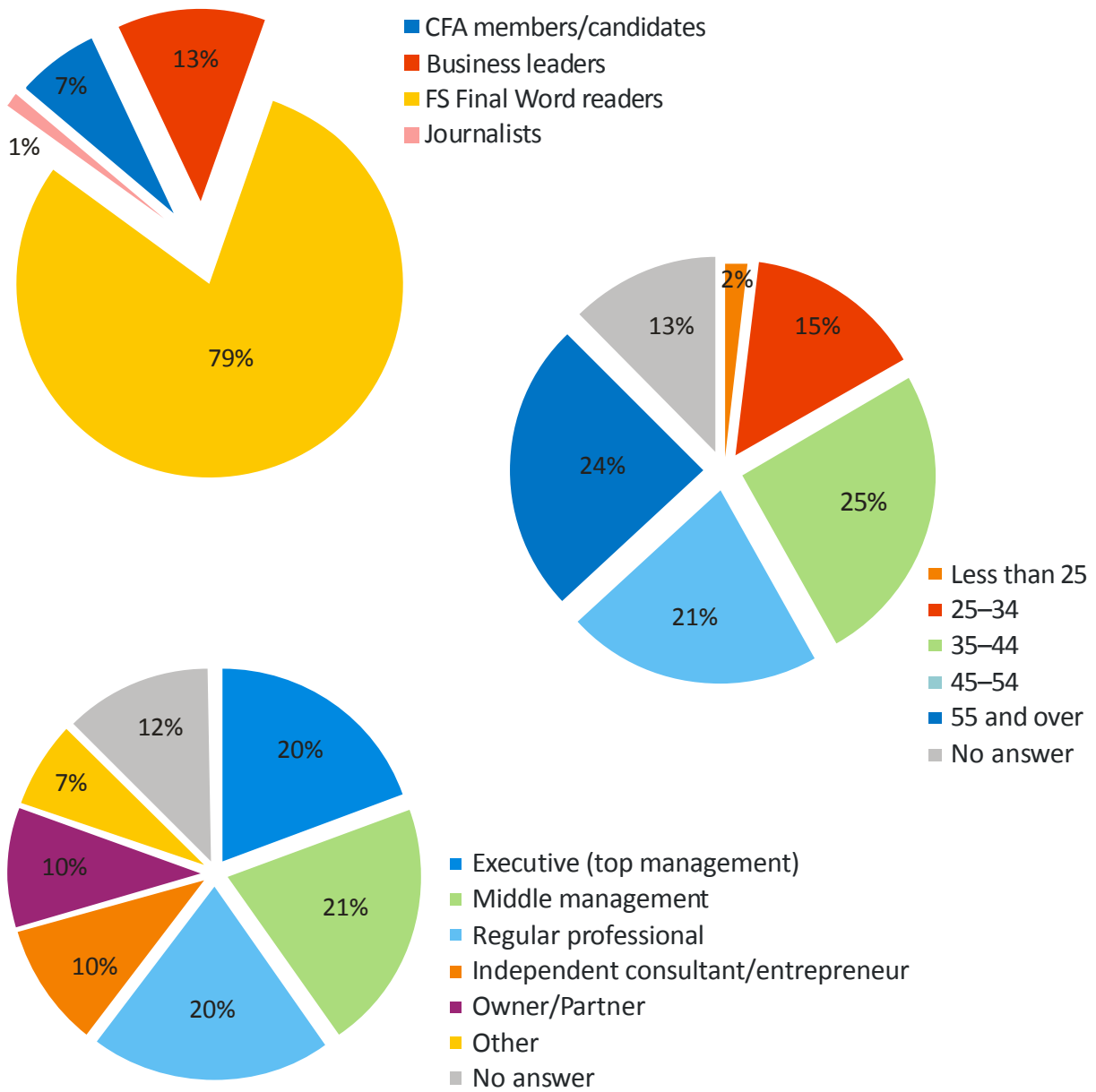
Most respondents expect positive yields from precious metals and commodities. Shares are not far behind.

The professional public has the lowest expectations for bonds and money-market instruments. Results obtained by the CFA Institute for the year 2013 worldwide show especially high expectations for shares that beat precious metals. Asia and Oceania express the greatest optimism for the rise of shares.

Our respondents foresee the highest yield from precious metals. It is worth mentioning that in mid-February 2013, the price of gold fell to under USD 1,600 per troy ounce for the first time in six months. In anticipation of economic recovery, investors purchased other assets. Some investors, however, remain optimistic about the long-term forecast for the yellow metal. They believe the world's economic issues have not been solved and that a new inflation wave may again push the price of gold higher.

Regarding commodities, prices went up in January 2013 after a long period. The commodity index DJ – UBS gained 2% this month. The U.S. stock index S&P 500 gained 6% in January 2013, jumping to its highest level since 2007.

Structure of respondent sample (%)



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