PFI Monthly

Delivering Knowledge That Matters.

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Content

Financial markets monthly dashboard

Source: Bloomberg; Michal Stupavský, CFA

	January	12 months change	Last value
Dollar index DXY	-0.1%	4.9%	108.37
EUR/USD	0.1%	-4.2%	1.036
EUR/CZK	-0.1%	1.1%	25.17
USD/CZK	-0.1%	5.6%	24.21
Global stock markets (MSCI All Country World)	3.3%	18.9%	
Developed stock markets (MSCI World)	3.5%	19.7%	
Emerging stock markets (MSCI Emerging Markets)	1.7%	12.0%	
Frontier markets (MSCI Frontier Markets)	0.8%	1.8%	
Global stock markets - Value (MSCI All Country World Value)	4.1%	12.9%	
Global stock markets - Growth (MSCI All Country World Growth)	2.6%	24.9%	
Global stock markets - Large Cap (MSCI All Country World Large Cap)	3.2%	19.9%	
Global stock markets - Mid Cap (MSCI All Country World Mid Cap)	3.8%	13.6%	
Global stock markets - Small Cap (MSCI All Country World Small Cap)	2.5%	11.6%	
US (S&P 500)	2.7%	24.7%	6041
US (Magnificent 7)	2.5%	68.0%	
US (S&P 500 Equal Weighted)	3.4%	15.7%	
US (NASDAQ)	1.6%	29.4%	
Non-US stocks (MSCI All Country World ex-US)	4.0%	8.1%	
Europe (STOXX Europe 600)	6.3%	11.1%	
Japan (MSCI Japan)	0.1%	9.3%	
Emerging Asia (MSCI Asia ex-Japan)	0.6%	16.8%	
China (MSCI China)	0.9%	30.5%	
India (MSCI India)	-2.5%	9.1%	
Latin America (MSCI Latin America)	9.4%	-20.0%	
Central Europe (CECEEUR)	9.8%	19.3%	
Czech Republic (PX)	6.3%	28.8%	1871
Global bond markets (Bloomberg Global-Aggregate)	0.6%	0.3%	
Global government bonds (ICE BofA Global Government index)	0.5%	-2.0%	
US Treasuries (Bloomberg US Treasury index)	0.5%	1.4%	
US Treasuries with maturity over 20 years (Bloomberg US Treasury 20+ Year index)	0.3%	-5.1%	
Global investment grade corporate bonds	0.6%	2.3%	
Global speculative grade corporate bonds (high-yield)	1.4%	10.9%	
EUR investment grade corporate bonds	0.5%	5.1%	
EUR speculative grade corporate bonds (high-yield)	0.6%	8.4%	
Czech government bonds (Bloomberg Czech Govt All > 1 Yr Bond)	1.4%	3.5%	
Average global bond yield (Bloomberg Global-Aggregate Yield To Worst)	-0.02%	0.07%	3.66%
US 10 year government bond yield	-0.03%	0.63%	4.54%
US 2 year government bond yield	-0.04%	-0.01%	4.20%
Germany 10 year government bond yield	0.09%	0.29%	2.46%
Germany 2 year government bond yield	0.04%	-0.31%	2.12%
Czech Republic 10 year government bond yield	-0.23%	0.12%	3.99%
Czech Republic 2 year government bond yield	-0.09%	-0.74%	3.36%
Average global investment-grade credit spread	-0.04%	-0.26%	0.85%
Average global high-yield credit spread	-0.22%	-1.26%	3.07%
Global commodity markets (Bloomberg Commodity Total Return)	4.0%	9.1%	
Crude oil Brent	2.8%	-6.1%	77
Copper	3.2%	5.0%	8954
Gold	6.5%	37.3%	2813
Silver	10.3%	39.3%	32.3

Interview

Jonáš Kotyza, Founder & Chairman of the Board, Prague Finance Institute

You founded Prague Finance Institute in 2019. What were your key ambitions and targets with this project back then?

PFI was founded on the belief that only by bringing together the brightest minds in the industry and sharing valuable information and knowledge can we achieve results that will enable us to succeed in a rapidly evolving economic environment. We felt that there was no community in finance and economics that could provide this, so together with our team, we decided to establish PFI.

Back in 2019, our key ambition was to create a platform that would bridge the gap between academic knowledge and real-world financial expertise. Another important goal was to establish PFI as a respected institution that would contribute to the professionalization of the finance sector in the Czech Republic. By organizing high-level discussions, networking events, and educational initiatives such, we aim to provide access to insights from global financial markets, investment strategies, and economic trends.

Last but not least, it is worth mentioning that we were inspired by the activities of the Prague Wallstreet Club, which has succeeded in creating a very interesting community of people. However, the club ceased to operate in 2018 and we have loosely built on it with PFI.

How would you evaluate the Institute's development since its foundation? Which major milestones have you managed to achieve?

Since its foundation in 2019, the Prague Finance Institute has grown significantly in both reach and impact (today we have 7.2 thousand organic followers on LinkedIn and 11.4 thousand subscribers on YouTube). I believe that our initial vision of building a strong network of finance professionals and fostering knowledge-sharing has materialized, but we continue to expand our activities.

One of the important milestones has been the successful establishment of PFI Talks, a flagship podcast series where we bring together leading experts from economics, banking, investment management, and private equity. These podcasts have become a platform for meaningful discussions on financial markets, macroeconomic trends, and emerging investment opportunities. We are proud to have hosted some of the most influential voices in the industry (Daniel Kahneman, Paul Krugman, David Petraeus, Aswath Damodaran, etc.), making PFI Talks a respected series in the domestic financial community.

We are also proud of the continuous development of our Masterclasses, which provide deep dives into specialized financial topics led by industry professionals, such as our flagship Business Valuation Masterclass. These sessions have evolved to offer even greater practical value, equipping participants with insights directly applicable in their careers.

Another achievement has been the growth of PFI Monthly, our analytical publication delivering expert commentary on market trends, investment strategies, and key economic developments. I believe it has become a trusted resource for finance professionals seeking in-depth, data-driven perspectives.

We have also launched PFI Roundtable, a series of high-level panel discussions where top executives, investors, and policymakers engage in thought-provoking debates on critical financial and economic issues.

Other important activities of the Institute include the PFI Student Club and PFI Jobs, a platform for identifying top talent in the labor market.

Could you please elaborate on the major Institute's highlights of 2024?

There have been many significant developments, for which I am especially grateful to our great team. In addition to the complete rebranding and update of PFI's corporate identity, the organization of numerous high-profile events, and the continuous work to improve our current activities, I would particularly highlight the first year of the PFI Scholarship initiative. This program aims to support talented students from disadvantaged backgrounds in studying abroad. I am delighted that we have been able to support our first student and fund his tuition fees for an MSc program at the London School of Economics. This is an initiative I am personally very excited about, and I am really glad we were able to launch it. I firmly believe this was the first of many years to come.

Another major step for PFI in 2024 was the addition of Andre Chelhot, an experienced economist who now leads our macroeconomic team. His expertise is a huge asset in our effort to become a leading regional think tank focused on finance and economics.

What are the key Institute development goals for 2025?

In addition to improving our current activities, I can mention, for example, the launch of another Masterclass focusing on real estate valuation, which will involve real experts in the field. Another important plan is the PFI Lab project, which aims to provide Czech students with access to a Bloomberg Terminal. Unfortunately, this essential financial market data source is currently unavailable to Czech students, which is a great pity. It is also worth mentioning the continuation of the PFI Scholarship, which we have already fully funded thanks to our great partners.

Where would you like to see the Institute in five years, in 2030?

One thing is clear—the status quo is not an option. :-) The ultimate goal is to be a think tank with an international reach, bringing together the best talent in the field and providing a platform for expert discussions on topics that will shape the future of the Czech economy. I firmly believe we have the necessary prerequisites to achieve this, especially the amazing people on our team, who bring enthusiasm and dedication to pursuing this goal, often at the expense of their free time.

BIO

Jonáš works as an Associate Partner at BHM Group, one of the leading Czech-based investment firms. Prior to joining BHM, Jonáš worked in corporate finance advisory for six years. He has participated in various projects for both local and foreign clients, including a number of successful M&A deals, bond issues, and IPOs. He graduated from the University of Economics in Prague and attended study programs at the McCombs School of Business (Texas, USA) and the London School of Economics (LSE).

Global macro insight of the month

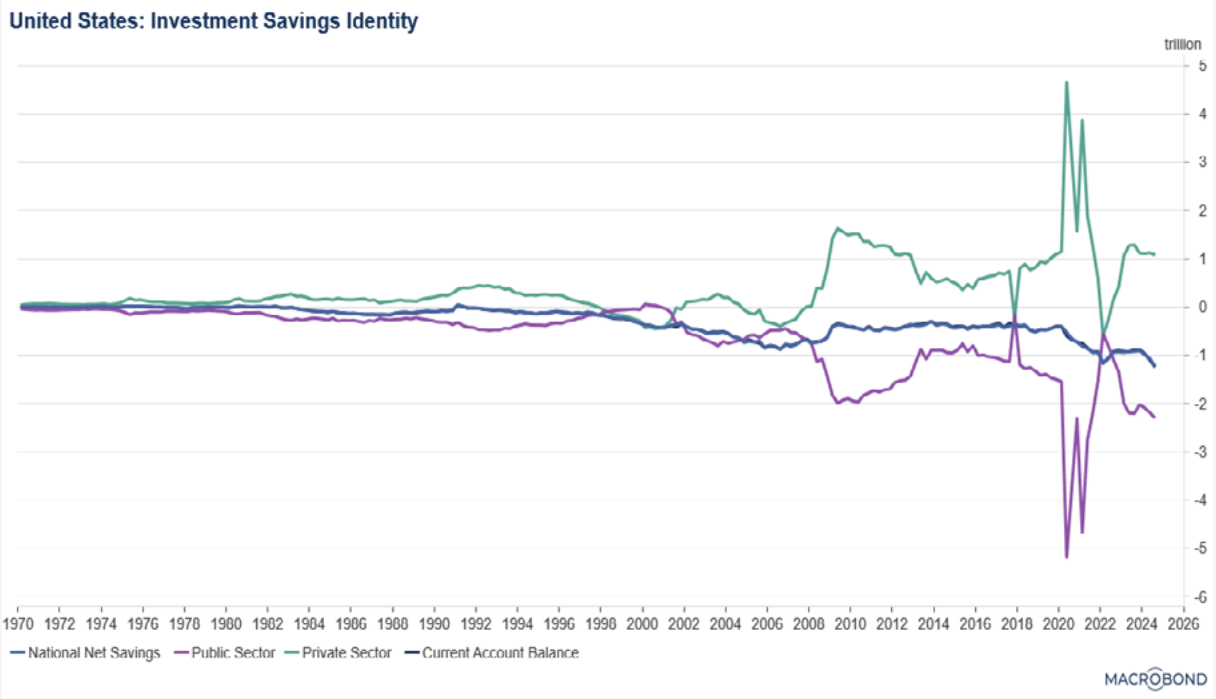
US trade and tariffs

Andre Chelhot, CFA

Chief Economist

The new set of tariffs imposed by the second Trump administration, if implemented in full, will have major implications for global inflation, exchange rates, and real interest rates, but their impact on global trade volumes will likely be more limited.

The U.S. economy is considered the consumer of last resort due to its dominant size and the high share of consumption spending in domestic demand. The chart below illustrates the investment-savings identity of the U.S. economy.



The chart shows that since 2008, the entire current account deficit can be explained by persistent, large budget deficits. This is what we call the twin deficits of the U.S., which must be funded by foreign capital to satisfy the balance of payments identity. Since the U.S. does not hold FX reserves—being in control of the world's reserve currency, the U.S. dollar—it relies on capital inflows to sustain these deficits.

Trump's policy aims to reduce the trade balance deficit and encourage the re-shoring of manufacturing activities. However, according to the above identity, a reduction in the trade balance deficit cannot occur without an increase in domestic savings, whether private or public. Given that the Trump administration is unlikely to pursue fiscal consolidation (such as raising income or corporate taxes), any improvement in the trade balance deficit would have to come from a rise in private savings—which implies a decline in consumption and investment spending while maintaining high national income growth. In other words, tariffs alone will not fundamentally resolve the trade balance deficit since they function largely as a transfer of savings from the private sector to the public sector. However, they could reduce the deficit at the margin, particularly through import substitution and supply chain adjustments over time. A more structural reduction in the trade balance deficit would require measures such as tax on foreign capital, import quotas, domestic production subsidies, or trade agreement shifts in addition to tariffs.

Impact of tariffs: Prices and exchange rates, not just trade volumes

The main impact of the proposed tariffs will come through prices and exchange rates, rather than through trade quantities. A key point to understand about tariffs is that, if applied universally, they function like a currency devaluation. For example, if the U.S. imposes a universal 10% tariff on all imports, it effectively means the real exchange rate of the U.S. dollar depreciates by 10% against its trading partners. These trading partners have multiple possible retaliation mechanisms:

1. Impose reciprocal tariffs on U.S. exports.
2. Devalue their currencies by 10%.
3. Absorb the tariff cost through profit margin compression.

Since most countries that trade with the U.S. run trade surpluses, they may have strong incentives to devalue their currencies to maintain their competitiveness. However, some countries might choose alternative responses, such as adjusting cost structures or absorbing some of the tariff impact.

We should note here that the Bank of Canada was the first central bank to halt its quantitative tightening (QT) program, and it has welcomed a weaker Canadian dollar (CAD), which has fallen to an all-time low against the USD amid uncertainty over trade relations with the U.S. This highlights a critical point: As long as capital remains freely mobile and exchange rates are floating, tariffs alone will not structurally reduce the U.S. trade deficit.

Short-term: The J-Curve effect & the dollar's role

In the short term, tariffs will cause a J-Curve effect—a temporary worsening of the trade balance before any adjustment occurs. This happens because:

- Tariffs make imports more expensive, but trade volumes take time to adjust as consumers and firms substitute costly imports with alternatives.
- The trade deficit may improve over time, depending on the price elasticity of demand for imports and exports.
- However, a stronger dollar—caused by global demand for U.S. assets—can exacerbate trade imbalances, making U.S. exports less competitive and imports cheaper.

These factors suggest that tariffs alone are unlikely to meaningfully reduce the trade deficit unless paired with policies affecting capital flows.

Capital flow restrictions: The real risk of trade wars

If tariffs or retaliatory measures escalate to the point where governments restrict capital flows, the real problem begins. The free movement of capital and open financial markets have allowed the U.S. trade deficit to be recycled into the economy as capital inflows, which has pushed down global real long-term interest rates over the past decades.

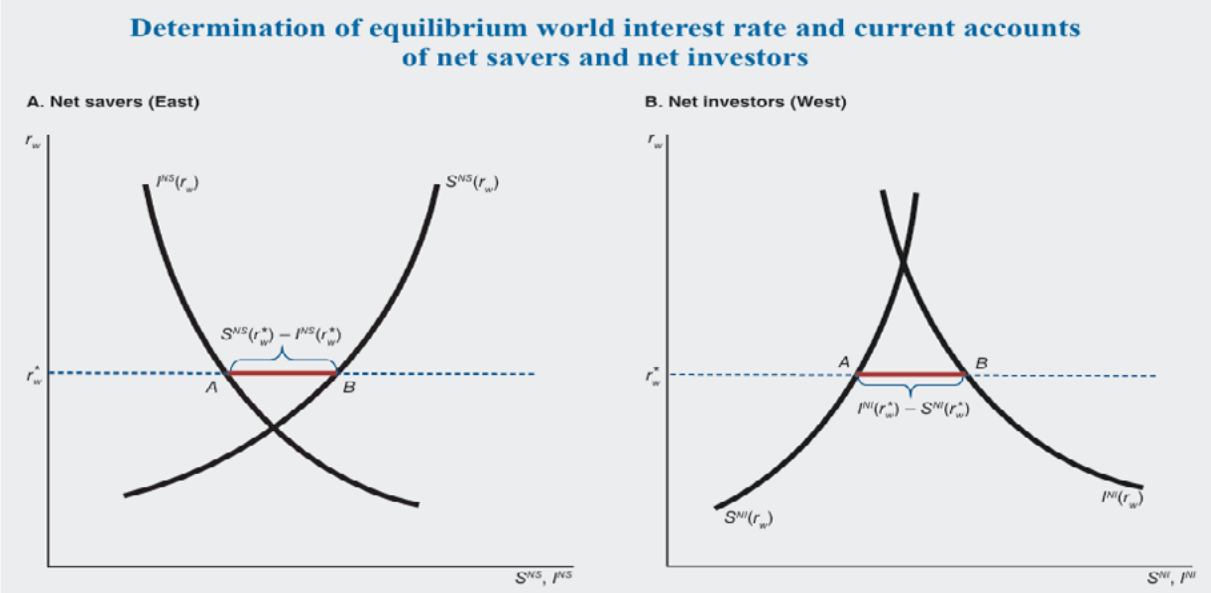
The mechanism is as follows:

- The world can be divided into two regions: the East (savers) and the West (investors).
- The global real interest rate rw* is determined by the equilibrium of desired savings (S) and investment (I) across these two regions:
- If the sum of global savings rises, while the sum of global investment falls, the equilibrium world interest rate rw*drops.
- The actual world real interest rate lies above the natural rate of the saver economies (e.g., China, Japan) and below the natural rate of the investor economies (e.g., the U.S.).

A shift toward restrictive capital flows would disrupt this equilibrium:

- Savers' economies (China, Japan) → Low rates due to excess savings.
- Investor economies (U.S.) → Higher rates due to funding constraints.

This divergence would result in higher real interest rates in deficit countries like the U.S., with potentially destabilizing effects on domestic investment and consumption.



Source: Robert Barsky, Matthew Easton, The Global Saving Glut and the Fall in U.S. Real Interest Rates: A 15-Year Retrospective, Economic Perspectives, No. 1, March 2021, Federal Reserve Bank of Chicago

Breakdown of the gold-TIPS correlation: A sign of fragmentation?

Until recently, gold prices and TIPS yields showed a negative correlation, since real yields represent gold's opportunity cost.

- Rising real yields made gold less attractive.
- Falling real yields made gold a more attractive store of value.

However, this relationship broke down after the U.S. and European countries seized the Russian Central Bank's assets in 2022. Since then, emerging market central banks have aggressively accumulated gold as a geopolitical hedge, reducing gold's sensitivity to real yields.

This shift suggests a growing fragmentation of the global financial system, with some countries diversifying away from dollar-based assets in response to the perceived risks of financial sanctions and capital flow restrictions.

Czech economy insight of the month

Czech economy finds itself in a stagnation

Ilona Švihlíková, PhD

Analyst

The Czech Statistical Office published preliminary data on the Czech economy conditions. The economic performance reached 1 % GDP growth in 2024, which is practically an economic stagnation. It is always useful to analyse the main GDP components to delve deeper into the economy.

The main driver of the economic growth was the household consumption, together with government institutions. The household consumption is the biggest GDP component in the Czech Republic, albeit much smaller than in most advanced economies. In 2023, a year stricken by high inflation, the ratio of household consumption to GDP amounted to little over 46 %. Usually it reached between 48-49 %. The household consumption revived given the rise in real wages, although very unevenly spread among sectors. However, it has to be said that based on year 2020 prices, the household consumption has not yet reached levels of year 2018. There is a potential for further growth in household consumption, however there are also high risks concerning the uncertain development in manufacturing industry and the corresponding increases in wages.

Negative influence stemmed mostly from gross fixed capital formation. This development reflects the negative sentiment of companies. The negative outlook is connected with high prices of energy (as the European Commission findings showed the electricity prices in the Czech Republic belong to the highest in the whole EU), lack of demand and overall downsize risks that might be connected with the new US administration and its inclination towards usage of tariffs. Overall, in the EU there are not many reasons for optimism, especially given the depressive outlook for the German economy.

Germany is the main trade and investment partner for the Czech Republic, and many Czech companies find themselves in Germany´s orbit. Given the unsatisfactory economic performance (-0.2 % in 2024, following -0.3 % contraction in 2023), the predictions for future remain gloomy. There have been many initiatives to restore export-led growth in the Czech Republic. However, there are many obstacles – the high energy prices hamper the competitiveness of Czech (more traditional industries). It is obvious that many companies are limiting their production, or even prepare for closure of factories, which means also massive layoffs (Spolana Neratovice). The export of the Czech Republic is highly concentrated – about 80 % of goods are destined for the EU, with the majority being delivered to neighbouring countries. Unfortunately, the Czech Republic has not been able to succeed in more dynamic markets of e.g. ASEAN countries, or central Asia.

The sectoral view of the gross valued added reveals that sector drivers in 2024 were retail, transport, hospitality sector – thus services, which is less typical for the Czech Republic. The decline of manufacturing underscores the depth of changes that are underway in the Czech economy, still mostly reflected in headlines of which company is shutting down its production, or shifting production abroad. Despite the unemployment rate being still low, there are visible increases in the number of people registered at the Labour office (and decreases in the number of vacancies).

Although the re-orientation to household consumption as the main economy driver could contribute to the increase in the standards of living, the other parts of such a shift are not "in place." Huge part of Czech workforce is employed in the manufacturing industry and the services sector is partly connected to it. The view of wages has been distorted for a long time – as the Czech Republic has been an export country, wages were mostly considered a problem (cost item), and not an important source of domestic demand. We can sadly observe the same thinking by the current government, which proceeds with policy that increases uncertainty for workers and dampens the wage growth.

The stagnation of the Czech economy is an important sign that the engines of growth need an overhaul. The government with its macroeconomic tools should present its view of future economic model – however that remains a wishful thinking.

Financial markets insights of the month

Are S&P 500 earnings poised for a mean-reversion?

Michal Stupavský, CFA

Head of Research

Jim Reid, Managing Director and Global Head of Macro Research and Thematic Strategy at Deutsche Bank, published the following impressive chart. The analysis shows that since 1935 S&P 500 EPS CAGR has been 6% and the difference between EPS CAGR and nominal GDP CAGR has been basically zero. However since 1995 the difference has become positive, i.e. higher EPS growth than nominal GDP growth, with the positive difference trending up based on the time-span since 2005 and even more so since 2015.

So during the last 10 years EPS has been on average growing faster than nominal GDP by 4 percentage points.

Is this mid-term trend poised for a mean-reversion to the long-term trend in the upcoming period or is it sustainable going forward? I would rather bet on the first option, although a precise timing is next to impossible of course. And I think at the same time that if the first option – the scenario of a gradual S&P 500 EPS dynamics mean-reversion – materialized during the upcoming period, S&P 500 valuations would have to significantly decline because their current rather frothy levels are in my opinion indeed pricing in a continuation of the current mid-term trend of significantly positive EPS-GDP growth difference.

Figure 1: Nominal and Real S&P 500 earnings growth since various dates with how much nominal earnings have outperformed nominal GDP from each period.

Source : Robert Shiller, Deutsche Bank

Financial markets insights of the month

The comeback of bond vigilantes and its impact on equities

Tomáš Pfeiler, CFA

Analyst

One of the key roles of global bond investors was to exert market discipline. They used to punish fiscal profligacy, and on the other hand, they rewarded fiscal restraint. However, the decade of ultra-low interest rates and the regime of abundant liquidity anaesthetised their natural instincts. Investors have become much less obsessed with deficits or overall debt levels – who would care if interest costs were virtually non-existent? Nevertheless, recent events show that after a period of hibernation, bond vigilantes are awakening.

First of all, holders of US government bonds have never bought the idea that the Fed should start the cutting cycle with an aggressive 50 bps move. There was no urgency for such a bold action. Fixed income asset managers started to "protest" in late September and as a result 10Y UST yield soared more than 50 bps within less than one month. Subsequent inflation and labour market data confirmed that bond market evaluated the situation correctly. US central bankers turned out to be wrong.

Other factor behind the recent bond investors' activism is Donald Trump's election victory. The republican president is largely known for his penchant for low taxes and pro-growth measures. While encouraging for the US economy in general, bond investors are much less impressed with these reflationary policies. They believe that growth is inextricably intertwined with inflation, and, unfortunately, the last inflationary episode which has started in 2021, is still live.

Such an outlook dissuaded the Fed from further cuts. The US central bank announced a pause in its easing campaign in its January gathering. Due to disappointment with the recent inflation figures, central bankers removed the reference to inflation making progress towards goal from its official statement. While an ostensibly innocuous change, it signals a broader policy shift. The Fed's pause will be longer – January was not just a skip. Therefore, another cut seems realistic in June at earliest. Furthermore, Trump's tariffs might have significant inflationary consequences. There are mounting concerns among institutional investors that the Fed may finally hold rates at current level for the entire 2025.

With rates staying higher for longer, deficits and debt levels are getting back into asset managers' radars. While Donald Trump believes his administration will rein in spending, most US government bondholders have serious doubts about that. Unfunded tax cuts are usually pronounced into elevated deficits. Therefore, most of the estimates suggests that deficit will be between 6 – 7 % in 2025.

We need to realize that the era of ultra-low rates has ended and the Fed has refrained from its role as the largest price agnostic buyer of the UST. In this new environment, the volume of deficit is no longer benign. Debt supply dynamics may therefore dictate price action in the UST market over the course of the year. Especially the preference of the new Treasury Secretary, Scott Bessent, for longer debt issuance might propel longer yields higher. With the 10Y UST yield sitting at around 4,5 % as of the end of January, the psychological 5 % level is quite easily attainable.

What are implications for equities and other risky assets? At current levels yields limit the potential for further valuation expansion, but they do not have to necessarily trigger a derating. Exceeding the psychological level of 5 %, a kind of pain threshold, however, might bring about sell-offs. At these levels of yields, fixed income securities are sufficiently attractive to spark the rotation from equities.

Some pockets of the market would be particularly vulnerable. Commercial real estate market is among the usual suspects – 10Y UST yields above 5 % might fuel large-scale defaults across sector. Under such circumstances, the US regional banks would suffer because they are disproportionately engaged with this segment of the real estate market. Thus, some broader financial calamity cannot be completely ruled out.

While such a scenario is not inevitable, investors should be more cautious. Equities are still in touching distance of the all-time high. It is far from certain than we will experience Lizz Truss moment in the US in 2025. Nonetheless, there is a plethora of factors, which might derail the recent bull run. High UST yields are prominent among them.

Financial markets insights of the month

Trade wars that may end with TR(I)UMP(H)?

Michael Schulz, CFA

Analyst

Market strategists and investors clearly remember 2018 and the disruptive trade wars between U.S. and China. A tit-for-tat battle initiated by Donald Trump during his first presidency clearly led to market volatility as he sought to redefine U.S. – China economic relations.

Now, in his second term, Trump has swiftly resumed economic confrontations, but this time with greater urgency, hoping to reposition United States within the global trade. Tariffs (at least the threat of them) seem to be an efficient way to make both U.S. allies and their trade partners, just as well as their rivals, sit to the negotiating table.

Financial markets, however, have not responded positively. On Monday, U.S. equities dropped sharply as they priced-in 25% tariff on Mexico and Canada, along with a 10% tariff on Chinese goods. Tariffs on Mexico and Canada seem to clearly be negotiating tactics as both countries' economies are to a significant degree reliant on trade with the U.S. Indeed, at the time of writing, tariffs on Mexico and Canada have been postponed by one month as both countries agreed to deploy military personnel to the border with the United States.

Tariffs on China, unlike other tariffs, will likely also mean a continuation of Trump's anchored geopolitical stance. China has already retaliated with imposing tariffs on LNG and coal. It remains to be seen whether Trump and Chinese president Xi Jinping will manage to find common ground later this week.

The economic consequences of the tariffs, should they be fully implemented, could be significant. Imposing tariffs could pose the exceptional U.S. growth at risk. Goldman Sachs estimates that every 5% overall tariff increase reduces earnings per share (EPS) by 200 to 300 basis points, while Citi warns that broad-based tariffs could shrink gross margins by up to 250 basis points.

What is more, a likely inflationary shock and consequently not-well-anchored inflation expectations may drive the yield curve and especially longer-term yields higher and potentially lead the U.S. dollar to edge to the 2022 multi-year highs. Strong dollar may further deepen the trade deficit of the United States.

Figure 1: 10Y yields have risen. Those correlate closely with DXY.

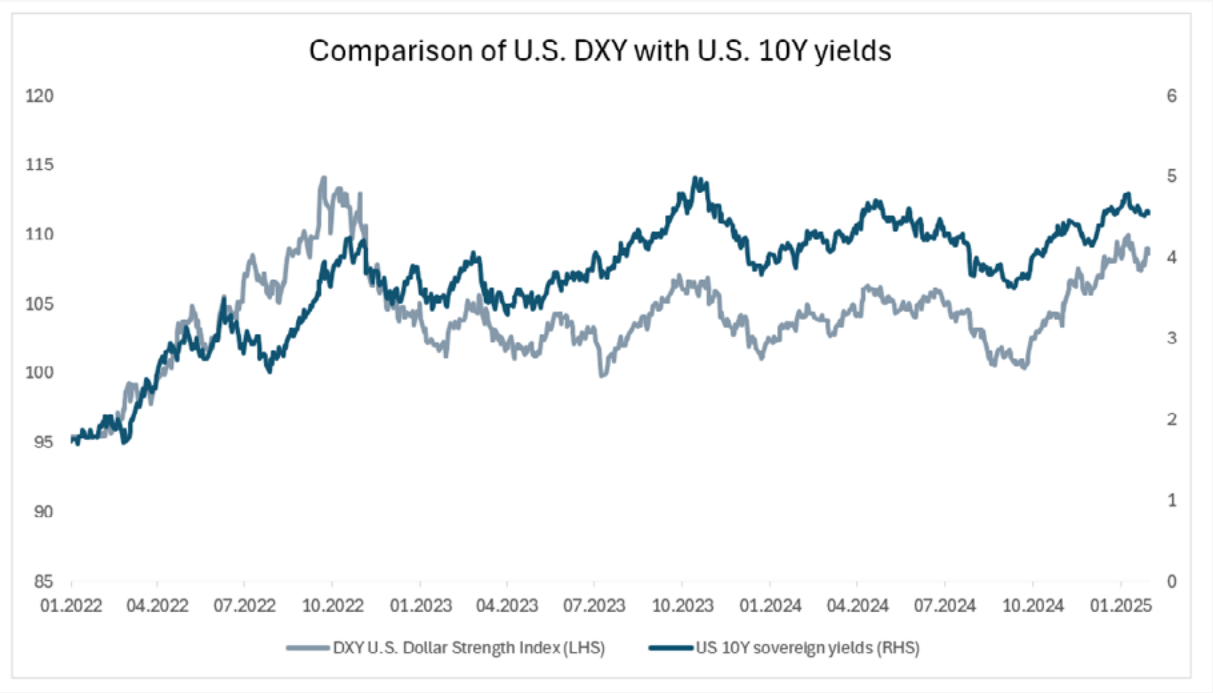
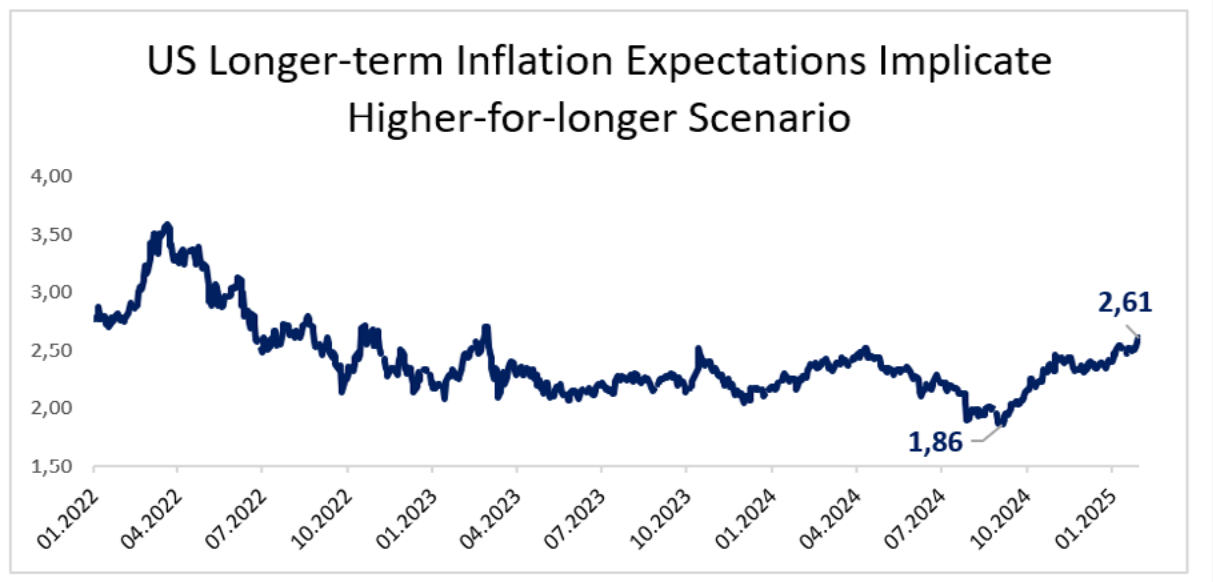


Figure 2: US 5Y breakeven inflation rate; Source: FRED



The U.S. economy now remains robust enough to absorb these shocks, should they not be too excessive. The same, however, cannot be said for Mexico and Canada. Those countries, due to their economic reliance on trade with the United States, could face significant slowdowns or recessions consequently. China, already grappling with economic slowdown, also finds itself in an increasingly fragile position.

Trump has launched his second term at a blistering pace, pursuing his agenda aggressively both across geopolitical and economic fronts. While some of his strategies may be grounded in legitimate concerns, others might be overly ambitious. Regardless, Trump has brought some of the key counterparties to the negotiating table, even though his methods are "somewhat" unconventional. The key question remains: how often will he manage to emerge victorious?

Banking sector insight of the month

The case against Bitcoin in central bank reserves

Michal Mesík

Analyst

The Governor of the Czech National Bank (CNB) continues to attract public attention. Recently, Ales Michl suggested in an interview with the Financial Times that the CNB could hold up to 5% of its reserves in Bitcoin. His idea is based on diversifying foreign currency reserves and increasing the profitability of the Central Bank's portfolio. According to CNB estimates, if the CNB had held 5% of its assets in Bitcoin over the past decade, its annual profits would have increased by 3.5 percentage points. The flip side is that the volatility of the returns would have doubled.

Let me explain why I believe that Mr. Michl's suggestion would be contradictory to the two key goals of the Czech National Bank: maintaining price stability (conducting monetary policy) and ensuring financial stability and the functioning of the financial system in Czechia.

In their conduct of monetary policy, central banks use reserves to inject or withdraw money from the banking system. In their quest to defeat inflation, central bankers sell government securities to reduce the money supply and thereby curb inflation. To conduct these so-called open market operations effectively, the central bank needs to hold high-quality, highly liquid assets on its balance sheet. In other words, it needs to be able to sell a large amount of assets relatively fast and without significant losses. Government bonds are the most suitable asset class for this purpose. Bitcoin, on the other hand, is far less liquid and more volatile compared to traditional assets like stocks and bonds. Consequently, the cryptocurrency would do little to support the implementation of efficient monetary policy. In addition, several central bankers, including Joachim Nagel, have recently warned about the dubious investment value of Bitcoin.

Another key goal of a central bank is maintaining financial stability. This involves providing emergency liquidity and buying up securities from commercial banks during periods of stress. Emergency liquidity can be financed either by printing money or from central bank reserves. Thus, during a crisis, it is even more important that central bank reserves remain liquid and of stable value. Bitcoin would make the reserves more volatile and less liquid. A logical consequence would be reduced trust in the ability of the CNB to support the financial system during stress periods—and not only during stress periods.

Trust in the central bank is a key ingredient of a stable financial system. Trust is created in interactions with commercial banks and underpinned by the quality of the CNB's holdings. The balance sheet of the CNB consists largely of foreign exchange reserves on the asset side, and commercial bank deposits and banknotes and coins in circulation on the liability side. Hence, central bank reserves effectively serve as collateral for commercial bank deposits (which in turn can be seen as collateral for individual client deposits). When money is transferred between commercial banks, central bank deposits act as a settlement platform. This requires trust from the banks that central bank deposits are secure and backed by central bank reserves. Now, imagine these reserves were held in Bitcoin. Could trust in the banking system be maintained in the light of a sudden sell-off of Bitcoin, as has happened several times in the past?

To sum up, a central bank is typically seen as the safest bank within the banking system—the lender of last resort. Its rating, or financial standing, is based on the riskiness of its balance sheet, which is determined by the central bank's risk appetite. Allowing a significant portion of Bitcoin on the balance sheet of the CNB, i.e., increasing the institution's risk appetite, would also increase the riskiness of the CNB's balance sheet.

Global M&A insight of the month

Johnson & Johnson to acquire Intra-Cellular Therapies in a $14.6 billion deal

Martin Bosák

Analyst

Johnson & Johnson (J&J) has announced plans to acquire Intra-Cellular Therapies (ITCI), a company focused on treatments for mental health conditions. The deal is worth $14.6 billion, with J&J agreeing to pay $132 per share, a 39% premium over its closing price on January 10, 2025 (as of February 2, ITCI shares trade at $127). The transaction is expected to close later this year, subject to regulatory approvals, approval by ITCI's stockholders, and other customary closing conditions.

ITCI is a biotech company that develops medicines for psychiatric and neurological disorders. Its most important product is Caplyta, an Food and Drug Administration (FDA)-approved drug used to treat schizophrenia and bipolar depression. A significant aspect of the deal is the recent patent settlement between ITCI and Sandoz, resolving litigation related to Caplyta. This agreement permits Sandoz to begin selling generic versions of Caplyta starting July 1, 2040, thereby potentially extending Caplyta's market exclusivity and bolstering confidence in its intellectual property durability.

ITCI and J&J both estimate that Caplyta could generate more than $5 billion in peak annual sales within the next 10 years. This is based on (i) growing use in bipolar disorder, (ii) expected expansion into major depressive disorder (MDD) treatment, and (iii) potential price increases over time. Besides Caplyta, J&J is also acquiring ITI-1284, a promising Phase 2 drug being developed for generalized anxiety disorder (GAD) and Alzheimer's-related psychosis and agitation. Experts predict ITI-1284 could generate over $1 billion in peak sales.

Financial analysts anticipate that the acquisition will be immediately accretive to J&J's revenue, with projected contributions of $663 million in 2025, assuming the deal closes by the end of the first quarter. This figure is expected to grow to $1.9 billion by 2028. J&J is using cash and short-term debt to finance the acquisition, but this will have a minimal impact on its financial stability since J&J is a $342 billion company with more than $20 billion in cash as of September 2024.

Investors appear to be enthusiastic about J&J's acquisition of this currently loss-making company, as J&J's share price has climbed 7% since the announcement. While the $14.6 billion price tag may seem high, J&J highlights the huge market potential, noting that 1 in 8 people worldwide lives with a neuropsychiatric or neurodegenerative disorder.

J&J's acquisition of ITCI is a strategic move to strengthen its position in mental health treatments. With Caplyta's growing sales and potential expansion into major depressive disorder, this deal aligns with J&J's goal of becoming the leading neuroscience company by 2030.

Czech M&A market insight of the month

Upvest and RSJ acquire 25% stake in Černý Most Shopping Center in a EUR 140M deal

Adam Friedl

Analyst

The new year in the Czech M&A market started slowly, with only six completed deals in January 2025, compared to 13 in the same month last year. Despite this slower activity, one transaction stood out—the acquisition of a 25% stake in Prague's Černý Most Shopping Center by Upvest and RSJ.

Upvest and RSJ jointly acquired the 25% stake in the third-largest shopping center in the Czech Republic for approximately EUR 140 million (around CZK 3.5 billion) from the French group Unibail-Rodamco-Westfield (URW). Upvest is a real estate investment platform specializing in structured financing for property projects, providing capital for residential and commercial developments while enabling investors to participate in real estate funding. RSJ is an investment group with a diverse portfolio spanning real estate, agriculture, and industry, focusing on acquiring income-generating properties and developing new projects. The agreement also includes an option to increase their ownership in the shopping center to up to 49% in the future. To complete the acquisition, they established a joint investment fund, which is set to open to additional qualified investors next year, facilitating the gradual increase of their stake in the shopping center.

Černý Most Shopping Center opened in 1997 as the first modern shopping mall in the Czech Republic. Over the years, it has undergone significant renovations and expansions, the most notable of which was completed in 2013. Covering nearly 85,000 square meters, the center features 176 retail units, a food court with 30 restaurants, and 3,000 parking spaces. Since mid-2024, the shopping center has been undergoing further expansion, which will make it the second-largest shopping mall in the country, second only to Westfield Chodov. Both centers are owned by the same French group, URW. The construction is expected to be completed by autumn 2025 and will add 20 new stores, 22 restaurants, and three additional cinema screens, representing an investment of approximately EUR 72 million (around CZK 1.8 billion).

The majority owner of Černý Most Shopping Center remains URW, a major owner, developer, and operator of premium commercial properties in Europe and the United States. The group manages 78 shopping centers across 12 countries, 45 of which operate under the Westfield brand. In the Czech Republic, URW owns and operates three major shopping centers—Westfield Chodov, Centrum Černý Most, and Metropole Zličín, all located in Prague.

The Czech M&A market continues to attract significant investments, particularly in the real estate sector. The recent acquisition of a stake in Černý Most Shopping Center underscores the ongoing interest of investors in prime commercial properties. As the year progresses, it will be interesting to see how such transactions shape overall market dynamics.

Private equity insights of the month

A way to invest in private equity

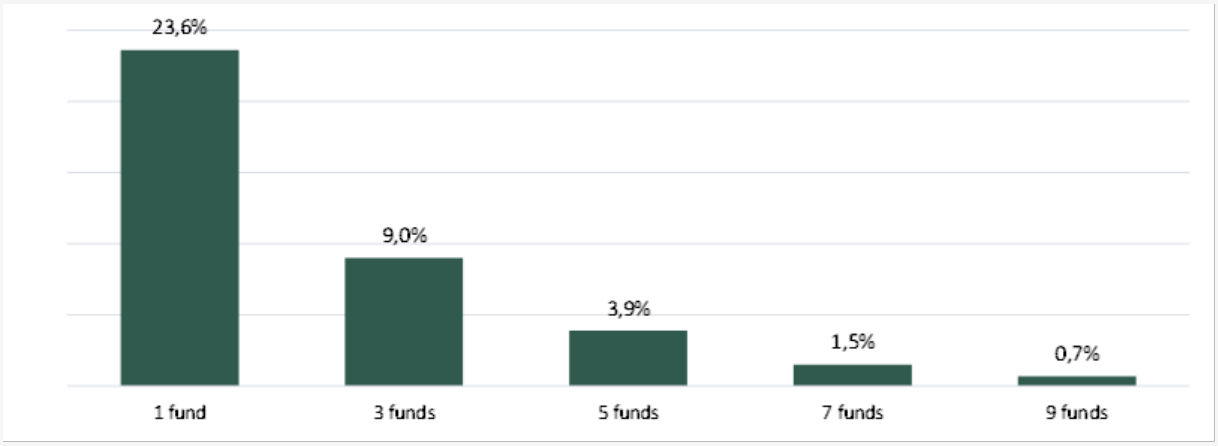
Diana Hricišáková

Analyst

In private equity, gaining access to top-tier funds can be challenging for individual investors due to high entry barriers and capital requirements. Many high-net-worth individuals (HNWIs) and smaller family offices aspire to invest in top-tier private equity funds but often face high minimum commitments and access limitations. This is where multi-family offices (MFOs) step in, pooling capital from multiple investors to build diversified private equity portfolios rather than relying on one-off investments.

One of the key benefits of this approach is access. Many top-performing private equity funds have limited capacity and prioritize institutional investors or large commitments. By aggregating capital, MFOs gain entry to these exclusive opportunities, offering their clients exposure to funds they might not reach on their own. Diversification is another major advantage. Instead of concentrating capital into just one or two funds, MFOs spread investments across multiple managers, strategies, and geographies, reducing risk and smoothing returns over time. As visible in the graph below, a portfolio consisting of just one private equity fund has a 24% probability of delivering a total value to paid-in capital (TVPI) below 1,0x, meaning a potential capital loss. However, by expanding the portfolio to nine funds, the probability of loss drops to less than 1%. This highlights how a structured, diversified approach significantly improves the chances of achieving positive returns.

Probability that the portfolio reaches TVPI < 1,0x (depending on the number of funds in the portfolio)



Source: Credit Suisse, Cambridge Associates

Additionally, MFOs provide professional fund selection and due diligence, leveraging deep industry expertise to identify top-performing managers. This institutional-level oversight helps mitigate risks and optimize portfolio construction. Beyond investment selection, MFOs handle administrative responsibilities, from performance monitoring to compliance, making private equity investing more accessible and manageable for their clients.

Despite these advantages, there are trade-offs to consider. One downside is cost—MFOs charge additional management fees on top of the underlying fund fees, which can eat into net returns. Investors must evaluate whether the access and diversification benefits outweigh these expenses. Another potential drawback is the loss of direct control. Investors partnering with an MFO give up direct control over decision-making, which may not suit those who prefer a hands-on approach in selecting funds or structuring co-investments. Lastly, private equity remains a long-term, illiquid investment, and while MFOs can structure commitments over time to optimize cash flows, investors still need to be prepared for extended capital lock-ups.

For investors looking to scale their private equity exposure without the challenges of direct fund selection, multi-family offices offer an attractive solution. By pooling capital, they unlock access to top-tier funds, enhance diversification, and provide professional oversight. While fees and control limitations are factors to consider, the benefits of a well-structured private equity portfolio often outweigh the drawbacks—making MFOs an increasingly popular gateway to private markets.

Private equity insights of the month

Global tensions attract investors

Lukáš Baloga

Analyst

The world's major superpowers are locked in a high-stakes game of geopolitical chess, with tensions reaching levels unseen in decades. From Russia's invasion of Ukraine to disputes in the South China Sea and escalating conflicts across the Middle East and Africa, the list of flashpoints is growing. As the U.S., China, and Russia navigate an increasingly volatile landscape, fears over global stability are mounting.

In response to escalating geopolitical tensions, global military expenditures soared to $2.44 trillion in 2023, marking a 6.8% real-term increase—the sharpest year-on-year rise since 2009.[1] Governments and alliances are ramping up defense investments, signaling a shift in strategic priorities.

The EU has introduced a €175 million equity fund aimed at attracting private sector capital into defense R&D[2], while NATO has launched a €1 billion Innovation Fund to support breakthroughs in AI, biotechnology, energy, propulsion, manufacturing, and space.[3] As instability grows, military and technological advancements are becoming critical battlegrounds for global power.

Why have investors stayed away from the sector?

Despite the recent surge in defense investment, many investors have traditionally steered clear of the sector due to high barriers to entry, limited scalability, and heavy reliance on government contracts. The defense market operates differently from commercial industries, with low unit volumes, complex procurement processes, and unpredictable government budgets adding layers of risk.

Large defense firms often depend on a few key customers and single large-scale programs, making revenue streams more volatile. Additionally, long R&D cycles and shifting political priorities create uncertainty, making it difficult for general and limited partners to commit capital. These challenges have historically kept many investors on the sidelines—until now.

Investment approach

KPMG's latest defense sector study highlights two main investment approaches: supply chain consolidation and technology-focused innovation.[4]

Supply chain consolidation

The ongoing consolidation of the aerospace and defense supply chain is creating major opportunities for long-term-focused private equity funds. For PE investors, this fragmented and distressed market presents a strategic opening to build scale through acquisitions and operational efficiencies. While short-term-focused funds may struggle with the sector's complexities, those with longer investment horizons stand to benefit from industry-wide shifts toward greater integration and stability.

Technology-focused innovation

A recent Deloitte survey found that 81% of aerospace and defense industry respondents are either utilizing or planning to incorporate AI and machine learning into their operations.[5] This technological shift is opening new investment avenues, allowing PE funds to capitalize on advancements that are poised to drive the sector's growth in the coming years. As defense strategies increasingly hinge on technological innovation, the commercial dynamics of the industry are undergoing a transformation, creating new opportunities for capital deployment.

The first swallows of venture capital in defense

Andreessen Horowitz has emerged as one of the most active investors in the defense space. Other major players— Franklin Venture Partners, Founders Fund, 8VC, Alumni Ventures, and Silent Ventures—are also fueling defense innovation, pouring capital into cutting-edge technologies that are reshaping modern warfare.

Opportunity?

As government defense spending rises and the digitalization of military strategies continues, the barriers to entering the sector are lowering. Private equity investors will increasingly focus on firms with proprietary intellectual property, strong customer relationships, and leadership in niche markets. These investors will play a crucial role in driving innovation and efficiency across the sector, reshaping modern defense technologies and ensuring sustainable growth in the industry.

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[3] https://tinyurl.com/vca3juvt

[4] https://assets.kpmg.com/content/dam/kpmg/xx/pdf/2021/07/the-private-equity-opportunity-in-defense-web.pdf

[5] https://www2.deloitte.com/us/en/insights/industry/aerospace-defense/aerospace-and-defense-industry-outlook.html.html

Real estate insights of the month

What does the rise in bond yields mean for CRE recovery?

Lukáš Štieber

Analyst

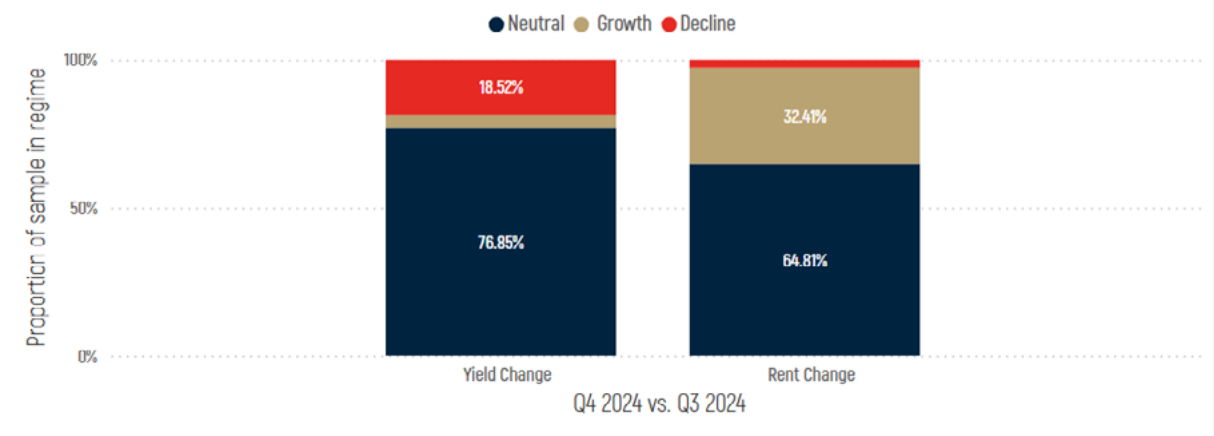
The latest European data on quarterly prime rent/yield dynamics from public CRE markets indicate mostly stable or improving in Q4 2024, as the quarter saw another rise in implied CRE capital values on average. The quarterly increase in private CRE capital values reinforces the overall market recovery in 2024, following a substantial decline in 2022–2023. However, the more volatile public CRE market, represented by REITs, experienced notable price declines, likely driven by the substantial rise in government bond yields over the past quarter. This trend suggests a sideways movement in privately held CRE prices.

Chart 1 illustrates the indicative market proportion of rent/yield dynamics driving capital value changes. Since rents and yields can increase, decrease, or remain unchanged, three regimes are considered: growth, decline, and neutrality. Based on data from three sectors across 36 European markets, 97% of sectors/markets experienced neutral or growing rent changes, while 95% saw neutral or declining yield changes. At the other end of the spectrum, 3% of sectors/markets reported declining rents, while 5% experienced rising yields. The overall magnitude of changes in rents and yields suggests a 2.1% quarterly increase in capital values, with a 95% confidence level of 0.0953%. Capital values rose by 3.1% for prime offices, 2.4% for industrial properties, and 0.86% for retail. Chart 2 indicates that most privately held CRE assets are on a stable or upward trajectory, in line with the prevailing narrative of "cautious optimism." The negative trend of falling rents is evenly spread across sectors, whereas rising yields are concentrated in the retail sector.

Rising (and elevated) bond yields following ECB rate cuts suggest a higher term premium on long-term government bonds. This aligns with expectations of a European GDP rebound in 2025, heightened political uncertainty across Europe, and the risk of higher inflation. However, the direction of bond yields remains uncertain—for example, the implementation of tariffs could weaken global and European growth, pushing government bond yields (DE10Y) lower.

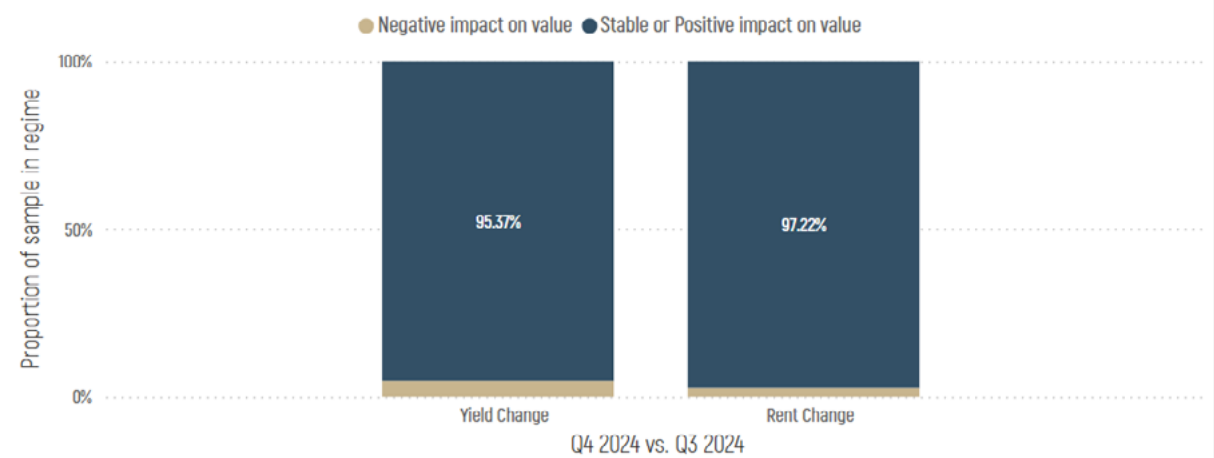
Against this backdrop, and with expectations of a modestly growing economy, the most probable trajectory for private CRE capital values remains consistent with the positive momentum observed in 2024. However, the pace of recovery will largely depend on economic growth—if the economy stagnates, CRE prices could lose their positive traction.

Chart 1: Yield and rent in the regime of neutral, growing or declining change (falling yields have positive impact on capital values)



Source: Arete (Data: C&W)

Chart 2: The stable or growing prime rent and stable or decreasing prime yield are dominating forces over Q4 2024 vs. Q3 2024



Source: Arete (Data: C&W)

Real estate insights of the month

Premium properties in the Czech Republic are being acquired by local investors

Peter Šulan

Analyst

Further improvement in economic conditions have created a perfect momentum for the Czech real estate market, leading to the completion of several significant transactions. All buyers involved in these deals are Czech investors, showcasing a clear trend – foreign capital is currently absent, with foreign investors choosing to allocate their funds in other markets.

In the last weeks, multiple high-profile real estate transactions across the Czech Republic have been announced:

- PPF Real Estate acquired the Prague Hilton hotel from the Irish group IBRC,
- Richard Morávek (via Max Realitní Fond) purchased the Atrium Flora shopping center from G City Europe as well as mix-use Myslbek palace from Anatol Invest Holding,
- Českomoravská nemovitostní acquired a portfolio of 16 office and retail properties from Redside,
- Upvest, in partnership with RSJ, acquired a minority 25% stake in Centrum Černý Most from Unibail-Rodamco-Westfield.

This shift in investor dynamics reflects broader trends in Central Europe, where foreign capital is increasingly flowing into Poland. With its larger market size, strong economic growth, and higher yields, Poland has become a more attractive destination for international investors seeking opportunities in the Central European region. Additionally, the perceived risks associated with Central European markets - ranging from regulatory changes to geopolitical concerns - have led foreign funds to concentrate on Poland more while largely bypassing the Czech Republic.

In 2024, the domestic capital greatly dominated the Czech real estate market, with iO Partners reporting that Czech investors accounted for 92% of total transactions. In contrast, Poland presents the opposite trend, as more than 90% of investment capital in its commercial real estate sector comes from foreign investors.

While foreign investors remain cautious about the Czech market and may favor other markets instead, local players continue to seize unique opportunities and further strengthening their presence by acquiring premium assets. The Czech real estate market remains highly attractive due to its positive economic outlook, generally low vacancy rates, and strong demand for premium office and retail spaces, which creates a safe and lucrative investment environment.

Behavioral finance insight of the month

The hidden value in financial decisions

Jana Přílučíková, PhD

Analyst

Meir Statman[1] once shared a story that highlights the difference between price and value. Imagine a man faced with the decision of whether to give his beloved a rose worth 5 euros or to hand her the same amount in an envelope. If he were thinking purely rationally, he might conclude that the rose will wither and eventually be thrown away, whereas the money could be used for something more practical or saved for the future.

From a rational perspective, the rose has no practical utility—it cannot be eaten or stored like money. However, choosing to give cash instead of the rose would likely not be well received by his wife. The act of gifting a rose carries an emotional message—it signals care, thoughtfulness, and affection. It allows the recipient to feel special.. The rose, despite its lack of practical utility, carries a message that cash could hardly replace. It is a symbol of thoughtfulness, a gesture that speaks volumes beyond its monetary worth.

This simple dilemma highlights an essential truth about human decision-making—our perception of value is not always dictated by price. It is shaped by emotions, social norms, and deeper psychological factors that extend beyond the realm of pure economics. That money has not only utilitarian properties, such as purchasing goods or saving, but also expressive and emotional aspects that shape perceived value.

For decades, traditional finance theory has assumed that market participants behave rationally. Rational behavior has long been defined by classical economics and finance principles, where individuals and firms make decisions aimed at maximizing utility. Traditional financial theory, rooted in neoclassical economics, presupposes that rational actors optimize utility, striving to maximize values aligned with their preferences. This perspective has served as a foundational pillar in financial literacy and economic education. However, behavioral finance challenges this assumption by highlighting how emotions, biases, and cognitive limitations frequently interfere with decision-making. Psychological factors help explain market anomalies, such as bubbles, overreactions, and inconsistencies in investor behavior, which traditional finance theories struggles to account for.

Price is merely an observable market outcome, whereas value is an internal assessment that varies based on personal experience, emotional state, and perception. By recognizing that financial choices are not always driven by pure logic, behavioral finance provides a more nuanced understanding of how individuals and markets operate beyond the confines of rationality.

During the 1970s and 1980s, traditional financial theories such as utility theory and the efficient market hypothesis were at their peak. However, anomalies in financial markets and repeated investor mistakes under uncertainty began to shake their legitimacy. In response, behavioral finance emerged as a dynamic field, integrating insights from psychology into economic and financial models.[2] [3]

The roots of behavioral finance can be traced back to the 19th century, with early works by Gustave le Bon ("The Crowd: A Study of the Popular Mind," 1896) and Selden ("Psychology of the Stock Market," 1912). However, the field gained significant traction in the late 20th century with contributions from psychologists and economists such as Daniel Kahneman and Amos Tversky, who introduced key concepts like heuristics, biases, framing, and prospect theory. Their work laid the foundation for understanding how individuals deviate from rational decision-making, particularly under risk and uncertainty.[4] [5] [6] [7]

The turning point came in 2002, when Daniel Kahneman was awarded the Nobel Prize in Economic Sciences for his work on prospect theory. Richard Thaler further advanced the field by introducing concepts like mental accounting and libertarian paternalism, earning him the Nobel Prize in Economic Sciences 2017.[8] While these contributions were instrumental, many other researchers have played significant roles in shaping behavioral finance, further challenging the long-held assumption of purely rational actors in markets.

Ultimately, behavioral finance underscores that financial decision-making is not purely logical but deeply intertwined with human psychology. The interplay between price and value is a testament to the complex nature of human behavior in financial markets, highlighting the necessity of incorporating psychological insights into economic and financial models.

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About

Prague Finance Institute (PFI)

Non-profit organization affiliated with CERGE-EI

PFI aims to connect experienced and young finance professionals, including students, especially through educational and networking events

Our key activities

- **PFI Macro Anchor podcast** hosted by PFI Chief Economist Andre Chelhot, CFA
- **PFI Talks podcast** in cooperation with the daily E15 (e.g. Daniel Kahneman, Jeffrey Sachs, Aswath Damodaran, Marc Faber, Barry Eichengreen or Peter Oppenheimer)
- **Panel discussions** (roundtables)
- **Valuation Masterclass** (semester-long business valuation course)
- **Technical Analysis Masterclass** (unique six lectures on technical analysis)
- **Research** (PFI Monthly magazine)
- **PFI Scholarship**
- **Platform for sharing interesting job opportunities** in the financial sector
- **Social media**, especially LinkedIn

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