C Forecast of the Development of Macroeconomic Indicators

C.1 Economic Output

Latest Development of GDP

Economic output, measured by real GDP, decreased by 0.9% (*versus 1.4%*) in 2013. Even though the economy emerged from a recession in Q2 2013, its growth was only limited.

Thanks to the planned increase in the excise tax on tobacco products, there was a considerable stockpiling of tax stamps for tobacco products in the last quarter. This was reflected in a high QoQ real GDP growth of 1.8% (*versus 0.5%*), whereas real gross value added, which does not capture direct effects of increases in indirect taxes, increased by only 0.8% QoQ. In a YoY comparison, real GDP increased by 0.8% in Q4 2013 (*versus a decrease of 0.7%*).

Domestic demand, due to an increase in final consumption expenditure and gross capital formation, and foreign trade balance both positively contributed to the QoQ increase in GDP. A positive sign was the fact that final consumption expenditure rose due to an increase in household consumption; nevertheless, for the time being it is hard to perceive this fact as a convincing sign of a turn-around. Similarly positive, although as far as the interpretation for the future is concerned somewhat inconclusive, information was a QoQ increase in gross fixed capital formation. In connection with recovery in the external environment, and thereby also in manufacturing, there was a considerable QoQ increase in exports.

In Q4 2013, YoY real growth in GDP was mainly driven by an increase in final consumption expenditure and partially also by the positive development of the foreign trade balance. Gross capital formation has slightly dampened GDP growth due to the development of inventories and valuables; however, after nine quarters it was possible to observe at least a slight increase in gross fixed capital formation. As for final consumption expenditure, private consumption also increased, although on a YoY basis the growth of government consumption was significant, too.

Specifically, in Q4 2013 household consumption increased by 1.0% YoY (*versus 0.5%*) and government consumption by 1.9% (*versus 1.2%*). In connection with the development of private consumption, we should point out that the CZSO has considerably increased the growth of household consumption in Q3 2013, from 0.5% in January to 1.3% at present. Real gross capital formation has decreased by 1.6% (*versus 5.3%*). This decrease was mitigated by an increase in gross fixed capital formation of 1.7% (*versus a decrease of 3.4%*).

In Q4 2013, real exports increased by 2.8% YoY (*versus 3.4%*), while imports rose by 2.5% YoY (*versus 3.4%*).

In Q4 2013, the real increase in household consumption was driven, in terms of its structure, by expenditure on semi-durable goods and also, for the first time in two years, by expenditure on non-durable goods. This could be caused primarily by two factors: by softening of the households‘ budget constraint or by an increase in consumer optimism (or decrease in pessimism), which would be reflected in a declining propensity to save. Given the negative development of compensation of employees and, on the other hand, the positive development of the consumer confidence indicator in the respective period, we incline to the second cause. For the whole 2013, household consumption was supported only by an increase in expenditure on semi-durable goods.

Investment in other machines, equipment and means of transport contributed to the real growth of gross fixed capital formation in Q4 2013. However, these signals are once again considerably ambiguous. This can be well seen in the data for the whole 2013, when gross fixed capital formation decreased in real terms, as did all major types of investment in physical capital.

In Q4 2013, foreign trade contributed positively to GDP growth amid an improvement in terms of trade. Real gross domestic income rose by 2.2% YoY (*versus 0.2%*).

In nominal terms, GDP increased by 3.1% (*versus 0.8%*) in Q4 2013. Considering the income structure of GDP, compensation of employees decreased by 1.5% YoY (*versus stagnation*). The main reason was a higher than expected fall in wage bill caused by the payment of extraordinary bonuses in Q4 2012 (see Chapter C.3). On the other hand, however, gross operating surplus increased by 4.9% (*versus 1.1%*).

The aforementioned nominal decline in compensation of employees undoubtedly represented a negative impulse for the development of real disposable income of households. On the other hand, the rise in gross operating surplus, which had been falling or stagnating in YoY terms since 2009, can be understood as a positive signal, one that both contributes to the growth of companies' internal resources and can also lead to an increase in their investment activity over time.

GDP Estimate and Forecast

Considering the development of business cycle statistics, foreign trade and the aforementioned positive signals in household consumption and gross capital formation, we assume that both domestic and foreign demand had a pro-growth impact in Q1 2014. At the same time, however, it is necessary to take into account the already mentioned one-off factor of stockpiling cigarette tax stamps, which conversely decreased quarterly GDP dynamics. Specifically, we estimate that on a quartlerly basis GDP decreased by 0.5% (*versus stagnation*). From Q2 2014, the quarterly growth of GDP should gently accelerate up to 0.5% (*versus 0.6%*) in the last quarter of 2014.

We estimate that GDP increased in Q1 2014 in real terms by 2.0% (*versus 1.0%*) on a yearly basis. Considering the revision of data on the development of household consumption in Q3 2013, we are adjusting the estimate of growth in Q1 2014 by 0.3 pp to 0.3%. We are not changing the estimate for government consumption growth of 1.0%. On the contrary, considering the surprising development in investment and taking into account the utilization of funds drawn from EU projects (detailed below), we estimate that gross fixed capital formation increased in real terms by 3.4% (*versus a decrease of 1.1%*) on a yearly basis. With regards to the recovery in foreign trade, we estimate that exports increased in real terms by 4.2% (*versus 3.8%*) and imports by 3.7% (*versus 3.2%*) on a yearly basis.

Compared to the January Forecast for 2014, we expect slightly more favourable development in the external environment, which is reflected in a slightly higher growth rate of the export markets. We also expect that the improving business cycle indicators will gradually be reflected in the decision-making of households and firms on their consumption and investment. This is confirmed, to a certain extent, by statistics from the individual sectors of the economy.

This year, real GDP could increase by 1.7% (*versus 1.4%*). The change compared to the last forecast is caused in particular by an increase in the forecast for growth in gross fixed capital formation. For 2015, we forecast GDP growth of 2.0% *(unchanged).* In both years, GDP growth should be attributed to domestic demand (approximately 66% both years).

In 2014, households will also be relatively more limited in terms of their incomes. We forecast that growth of real disposable income will only be limited. This follows from the low dynamics of nominal incomes, since growth in price levels will be low in spite of the CNB's foreign exchange interventions. The unemployment rate will fall only very slowly, and in comparison with 2013 there will only be slight employment growth. Against these factors, however, is the rapid decline in the pessimism of Czech households, which could mitigate the creation of prudential savings. For 2014, we forecast a growth in household consumption of 0.6% (*unchanged*). A relatively pronounced reduction in the forecast for growth in real incomes will be to a great extent compensated by a growth of household consumer appetite. In 2015, household consumption growth could accelerate to 1.5% (*unchanged*).

We estimate government consumption to grow by 0.8% (*versus 1.0%*) in 2014 and by 0.7% (*versus 0.4%*) in 2015 in real terms. The change in the forecast is related to a growth in consumption of medical services and changes in direct and indirect taxes in accordance with the government's programme statement.

In Q4 2013, the recovery of foreign trade was reflected in the development of investment in fixed capital as well as the low base of comparison as a result of a long-term decrease in selected investment components. Although investment in fixed capital is much more volatile than household consumption, and any slight growth must be interpreted with utmost prudency, we forecast its recovery in 2014. The primary reason is the fact that in Q4 2013 investment growth was also accompanied in by growth of gross operating surplus, which is the initial indicator of company internal resources. Secondly, in weighing up new information on opportunities to obtain resources in 2014 and 2015 from the EU financial perspective 2007–2013, we have increased the volume of gross fixed capital formation in current prices compared to the January Forecast to take into account the probable better utilization in these years. The risk of this estimate is, however, the rate at which private investment will be squeezed out. In 2014, gross fixed capital formation should increase by 2.7% (*versus a decrease of 0.3%*) in real terms, and by 2.0% (*versus 2.6%*) in 2015.

In 2014 and 2015, foreign trade will have a pro-growth impact. In 2014, real exports could increase by 3.8% (*unchanged*) and real imports by 3.4% (*versus 3.2%*). In 2015, we expect real exports to grow by 4.2% (*versus 4.0%*) and imports by 3.8% (*unchanged*).

In 2014, nominal GDP should grow by 3.6% (*versus 3.1%*). In 2015, we forecast nominal GDP growth of 3.7% (*versus 3.3%*).

C.2 Prices

Consumer Prices

At the beginning of 2014, YoY inflation slowed considerably in accordance with the January Forecast. This slowdown was caused by the fadeaway of the impacts of last year's increase in VAT and the fact that the YoY change in regulated prices switched from growth to decline.

YoY growth of consumer prices reached 0.2% (*in line with the forecast*) in February 2014. The contribution of administrative measures was –0.6 pp, of which 0.1 pp could be attributed to last year's increase in the excise tax on cigarettes and –0.7 pp to regulated prices. The decrease in regulated prices was particularly driven by a decrease in the electricity price of 10.5%.

When examining the contributions of individual segments of the consumer basket to YoY inflation in February 2014, food and non-alcoholic beverages (0.7 pp) contributed most. In contrast, growth in prices was mitigated mostly by housing (–0.7 pp).

In spite of the weakening of the koruna due to the CNB's foreign exchange interventions, **2014** should be characterized by very low inflation.

A breakdown of YoY inflation into the contributions of market and administrative effects (see Graph C.2.2) makes it clear that administrative measures should have an anti-inflationary effect in the course of 2014. The negative contribution of regulated prices will outweigh the positive contribution of changes in indirect taxes.

With regard to indirect taxes, the inflation forecast for 2014 expects an increase in excise taxes on cigarettes. The total contribution to the YoY growth of prices in December could be 0.3 pp, of which approximately a third could be attributed to an increase in the excise taxes effective as of 1 January 2014. The remaining 0.2 pp could be attributed to the expected increase in excise taxes resulting from the transposition of the European directive which, however, has not yet gone through the legislative process. The impact of these tax changes on consumer prices should be gradual and should be reflected mainly in H2 2014.

Based on the aforementioned assumptions, we expect that the contribution of administrative measures to the YoY growth of consumer prices in December 2014 will be zero (*versus –0.1 pp*), of which electricity should account for –0.4 pp. Unlike previous years, administrative measures will be an important anti-inflationary factor.

The negative output gap will also have an anti-inflationary impact, in spite of the solid QoQ growth of gross value added in Q4 2013. Another factor that should exert slight anti-inflationary pressure is the expected development of unit labour costs (see Table C.3.3). Inflation should be influenced only slightly by the US dollar crude oil price, where a slight decrease of 3.8% is expected. In contrast, one important factor driving up inflation is the weakening of the koruna due to the CNB's foreign exchange interventions. The expected YoY weakening of the koruna of 4.8% against the EUR and 3.2% against the US dollar represents relatively strong upward pressure on inflation. In addition to the contributions of administrative measures, this impetus also lies behind the expected acceleration of YoY inflation in the course of 2014, which apparently only reached 0.2% in Q1 2014, but should climb to 1.9% in Q4 2014.

Despite the considerably loose monetary policy, both in the exchange rate and interest rate components, the **average inflation rate in 2014** should be very low and reach only 1.0% (*unchanged*), with a YoY increase in prices of 2.0% (*versus 1.9%*) in December 2014.

In **2015,** administrative measures should already be acting in the usual pro-inflationary direction, in spite of the introduction of the third VAT rate of 10% and the abolition of fees for doctor visits, which together should bring inflation down by 0.2 pp.[4] Unlike this year, unit labour costs should have a pro-inflationary impact. Inflation should continue to be moderately mitigated by a slight decrease in the crude oil price, while the impact of the weakened koruna exchange rate should fade and the negative output gap should then dampen growth of prices less intensively than this year. We expect the average inflation rate in 2015 to reach 2.3% (*versus 2.4%*) and the YoY increase of consumer prices in December 2.0% (*unchanged*).

Deflators

The gross domestic expenditure deflator, which is a comprehensive indicator of domestic inflation, grew by 0.9% (*versus 0.5%*) YoY in Q4 2013.

In terms of its structure, the growth was a result of both an increase in the household and government consumption deflator and an increase in the gross capital formation deflator. Growth of the gross fixed

[4] *In relation to the government's programme statement, we expect the introduction of this rate for selected representatives of the following consumer basket segments: health, recreation and culture.*

capital formation deflator as well as the household consumption deflator was influenced, to a certain extent, by the CNB's intervention; nevertheless, with regard to the intervention timing, prices have not yet fully adjusted. Investment demand is too weak for the time being to consider demand factors.

In Q4 2013, the terms of trade showed a growth of 1.8% (*versus 1.1%*). Both export and import prices were affected by the depreciation of the Czech koruna.

The implicit GDP deflator, which is a result of the gross domestic expenditure deflator and the terms of trade, increased on a yearly basis by 2.3% (*versus 1.5%*) in Q4 2013. From the above, it should be clear that this discrepancy (forecast vs. data) originated due to the relatively strong improvement (growth) of the terms of trade and the higher growth of the gross domestic expenditure deflator, mainly due to a relatively higher growth of the gross fixed capital formation deflator.

The gross domestic expenditure deflator could increase by 0.8% (*unchanged*) in 2014 and by 1.4% (*versus 1.7%*) in 2015. The terms of trade should post a growth of 1.2% (*versus 0.9%*) in 2014, while for the following year we forecast an increase of 0.5% (*versus a decrease of 0.2%*). We take into account a higher growth of the deflator of exports of goods in both years. In 2014, it should be a consequence of both the impact of the depreciation of the koruna exchange rate and a lower than previously (in the January forecast) expected decrease in reached prices. In 2015, we now expect reached prices to grow. In reaction to the koruna exchange rate development in Q1 2014, we have slightly increased the forecast for the growth of the import deflator, while the forecast for 2015 remains almost unchanged.

In relation to these values, we forecast growth of the implicit GDP deflator of 1.8% (*versus 1.7%*) in 2014 and we expect it to increase by 1.7% *(versus 1.3%)* in 2015.

C.3 Labour Market

The behaviour of the labour market continued to be somewhat non-standard from the macroeconomic perspective. YoY growth in headcount employment continued. In line with expectations, the number of registered unemployed rose, although unemployment (LFS) decreased. Considering the shift of bonuses and the growing number of part-time jobs, a decrease in wages was expected, although its extent was rather surprising.

Employment

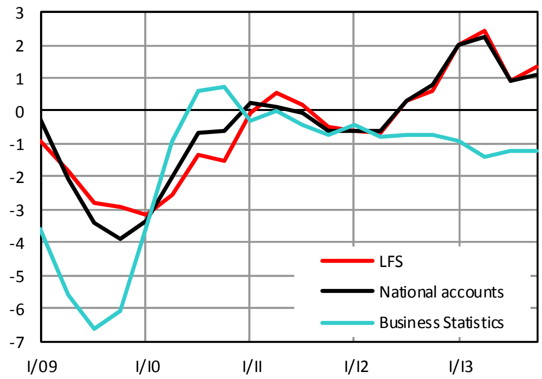
According to the LFS, **employment** grew by 0.8% YoY (*versus 0.5%*) in Q4 2013, mainly due to an increase in the number of employees of 1.3% (*versus 0.7%*). The biggest contribution to this result came from the tertiary sector.

Employment dynamics was significantly affected by a YoY increase in the share of part-time jobs, mainly in retail and education. From the demographic point of view, women aged 25–49, above all, contributed to this increase. This could be an evidence that labour supply is still elevated as households want to secure extra income.

As far as the employment structure by professional status is concerned, signs of a gradual reversal from the previous quarter were confirmed. The number of self-employed continued to fall on a yearly basis, while the number of employers increased slightly.

Employers' efforts to increase labour productivity should lead to effective stagnation of employment. Employment should increase by only 0.2% (*versus 0.1%*) in both 2014 and 2015, in spite of a gradual economic recovery.

Graph C.3.1: **Employees in Different Statistics**
YoY growth rate, in %, business statistics in full-time equivalent



Source: CZSO

Since mid-2010, **employment rate** of the population aged 15–64 has been showing continuous growth. In Q4 2013, it increased further by 1.2 pp YoY (*versus 1.0 pp*), especially due to the increasing share of part-time jobs.

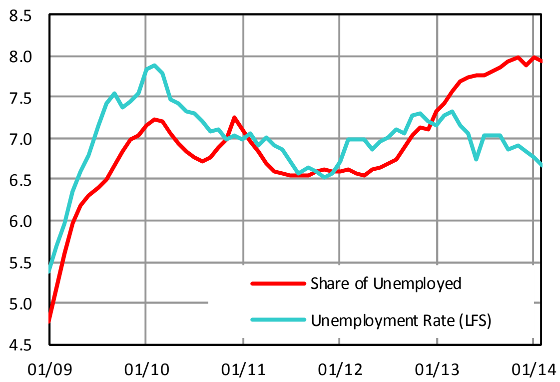
Economic activity rate (15–64 year-olds) grew by 1.0 pp YoY in Q4 2013 (*versus 0.9 pp*). This growth continues to reflect in particular the increased motivation of households to compensate for a decrease in real disposable income by means of formal and informal gainful activities.

Changes in the demographic structure, apart from the increase in work activity, have considerably contributed (and will continue to contribute in the next few years) to the increase in participation rate (see Chapter A.5).

Unemployment

In the EU context, the unemployment rate (LFS) in the Czech Republic is one of the lowest. On the other hand, the number of job applicants registered at labour offices in 2013 has reached its highest level in the Czech Republic's history, and a further increase can also be expected in 2014. Economic interpretation of these indicators, the development of which is shown in Graph C.3.2, follows from their definition. Registered unemployment in the current situation is an expression of the continuing strong motivation towards any extra income, while registration at labour offices is also a condition for being granted a number of social benefits. According to the current legislation, partial extra earnings are supported or at least tolerated within the framework of the registered form of unemployment (for LFS, this is entirely excluded by definition), which results in stagnation or a slight decrease in the LFS unemployment rate.

Graph C.3.2: **Indicators of Unemployment**
seasonally adjusted data, in %



Source: CZSO, Ministry of Labour and Social Affairs, own calculations
Note: Share of unemployed (Ministry of Labour and Social Affairs) is defined as a share of available job seekers aged 15 to 64 years in the population of the same age.

Seasonally adjusted **registered unemployment** in February 2014 already decreased, while a positive factor is the growing number of registered unemployed who found jobs independently. The share of unemployed persons (seasonally adjusted) could reach its peak during 2014; however, pressure on higher levels of registered unemployment will persist.

The **LFS unemployment rate** reached 6.7% in Q4 2013. A decrease in the long-term unemployment rate contributed to its slight QoQ decline. If this trend is confirmed, it would mean a positive signal from the perspective of developments in structural unemployment, which could contribute to a stronger response of the unemployment rate to an improving position in the economic cycle. However, for 2014 we still expect only a slight decrease in the unemployment rate of 0.2 pp. We assume a more intensive utilization of core employees, to a lesser extent supplemented by agency employees, which means that the job finding rate could remain dampened.

Wages

The extent of the decrease in the wage bill and the average wage in Q4 2013 was rather surprising.

The **wage bill** (national accounts methodology, domestic concept) showed a considerable decrease of 2.7% (*versus 0.3%*) in Q4 2013. This can partially be attributed to the extent of managerial bonuses shifted to Q4 2012 as a result of the introduction of the solidarity surcharge for income tax from 1 January 2013. An increase in the number of part-time jobs could also have had an impact on the decrease in the wage bill in Q4 2013. The structure of part-time jobs indicates that their hourly remuneration could be lower compared to standard forms of employment. A dominant factor behind the relatively low growth of wages in 2014 should be the private sector's efforts to compensate for a continuous decrease in net operating surplus from 2009 to 2012. An increased proportion of employment in the informal sector, to which the divergence between registered and LFS unemployment as well as between LFS employment and employment according to the business employment statistics point, could further contribute to low wage growth.

The wage bill could therefore increase by 1.7% (*versus 2.2%*) in 2014 and by 3.6% (*versus 4.3%)* in 2015. Based on the government's decision, 2 pp of the health insurance rate will not be transferred from employers to employees from 2015. According to our original estimates, the contribution of this change to wage bill growth should have reached 0.5 pp in 2015.

In Q4 2013, **the average wage** (business statistics, full--time equivalent) decreased by 1.8% (*versus an increase of 0.8%*), in real terms it decreased by 2.9%. The impact of Q4 2012, when a considerable amount of extraordinary bonuses was paid out, is also important in this statistics. For the reasons mentioned in previous paragraphs, we expect the average wage to grow by 2.1% in 2014 (*versus 2.5%*) and by 3.4% in 2015 (*versus 4.2%*).

C.4 External Relations

(balance of payments methodology)

In 2013, the external imbalance, expressed as a ratio of the current account balance to GDP, reached –1.4% (*versus –1.7%*), thus deteriorating slightly by 0.1 pp in annual terms. The income balance deficit widened by 1.3 pp and the surplus of the balance of services decreased by 0.3 pp. On the other hand, the trade balance surplus increased by 1.0 pp and the balance of current transfers, moving from deficit to surplus, also improved by 0.5 pp.

The analysis of the previous development of the balance of payments and its forecast were influenced, to a certain extent, by the data revision conducted by the CNB upon the publication of data for Q4 2013. The revision covered the data for 2012 and the first three quarters of 2013; all parts of the current account and some items of the financial account were revised. In 2012, the income balance improved by CZK 29 billion, the balance of services by CZK 12 billion and the goods trade balance by CZK 3 billion. The ratio of the current account balance to GDP improved due to the revision by 1.1 pp to –1.3% in 2012; by contrast, in the first three quarters of 2013 it deteriorated by 0.3 pp to –2.0%.

Export markets[5] started growing again during 2013, after their two-year decline, and they increased by 1.2% during the whole year (*versus 0.9%*). The expected recovery of the global economy should be favourably reflected in export market dynamics. Export markets could increase by 3.3% in 2014 (*versus 3.1%*) and by 3.1% in 2015 (*unchanged*). This should be positively reflected in the foreign trade results.

Export performance, which indicates a change in the share of the volume of Czech goods on foreign markets, was lower by 0.2% in 2013 (*versus stagnation*). Improved price competitiveness of Czech firms resulting from a weaker exchange rate of the Czech koruna (in connection with the CNB's foreign exchange interventions) should contribute to an increase in export performance of 0.8% in 2014 (*versus 1.0%*) and by 1.2% in 2015 (*versus 1.0%)*.

In 2013, foreign trade in goods was recovering only slowly from its decline caused by weak foreign and domestic demand. The volumes of exports and imports started rising as late as in the second half of the year when growth rates were gradually increasing. For the larger part of the year, exports were growing faster than imports, which led to the trade balance surplus reaching record highs.

In 2013, the trade balance surplus reached 4.8% of GDP (*versus 4.9%*). It could increase to 6.1% of GDP (*versus 6.2%*) in 2014, partially thanks to the continuing positive impact of the terms of trade. In 2015, trade balance surplus could reach 6.9% of GDP (*versus 6.2%*).

The deficit in the fuel balance (SITC 3) reached 5.2% of GDP in 2013 (*versus 5.1%*). With regard to the expected scenario for crude oil prices and the development of the koruna exchange rate, we assume that in the course of 2014 and 2015 the deficit in the fuel balance will roughly stagnate or slightly decrease. It should reach 5.0% of GDP (*versus 4.9%*) in 2014 and 4.6% of GDP (*unchanged*) in 2015.

Imports of services have been increasing in the last three years at a higher pace than exports of services, and thus the surplus of this part of balance has gradually been decreasing. Worse YoY results of the balance of transport services and the balance of tourism participated roughly equally in a decrease in the overall surplus in 2013. The surplus in the balance of services reached 1.4% of GDP in 2013 (*versus 1.3%*). The impact of the improvement in external environment or the weaker koruna could bring at least a small increase in the surplus in the balance of services in the following period, yet the balance of services should in relative terms remain almost unchanged. We expect the surplus in the balance of services to reach 1.4% of GDP in 2014 and 2015 (*in both cases unchanged*).

The deficit in the income balance, which includes the reinvested and repatriated earnings of foreign investors, deepened in 2013 compared to the previous year by 1.3 pp, reaching 8.0% of GDP (*versus 7.9%*). The increase in the deficit was largely due to an increased outflow of investment income in the form of dividends paid out to foreign owners of domestic direct investments. The balance of compensation of employees improved, though it has had a much lower impact on overall income balance. We expect that the deficit in the income balance will continue to grow and will reach 8.2% of GDP in 2014 (*versus 7.9%*) and 8.8% of GDP (*versus 8.1%*) in 2015.

[5] *Weighted average of the growth of goods imports by the six most important trading partner countries (Germany, Slovakia, Poland, France, United Kingdom, and Austria)*

We assume that in 2014 the current account balance will improve considerably to –0.4% of GDP (*versus –0.2%*), mainly due to the favourable development of foreign trade in goods. The current account balance should remain at a similar level also in 2015, when it could improve slightly to –0.3% of GDP (*versus –0.4%*). In both years, the current account of the balance of payments should thus be nearly balanced.

C.5 International Comparisons

Comparisons for the period up to and including 2013 are based on Eurostat statistics. Since 2014, our own calculations have been used on the basis of real exchange rates.

Using the purchasing power parity method, comparisons of economic output for individual countries within the EU are made in PPS (purchasing power standards). PPS is an artificial currency unit expressing a quantity of goods that can be bought on average for one euro on EU27 territory after converting the exchange rate for countries using currency units other than the euro. Using Eurostat data, the purchasing power parity of the Czech Republic in 2013 was CZK 18.14/PPS compared to the EU27, or CZK 17.41/EUR compared to the EA12.

Due to the recession, GDP per capita measured in **current purchasing power parity** declined in 2009 in all monitored countries, with the exception of Poland. While most states have gradually recovered from the crisis, in Greece the absolute economic level continued to fall without interruption until 2013. The absolute economic level also decreased slightly in Croatia in 2010 and 2013, in Portugal in 2011 and 2012 and in Slovenia in 2012 and 2013. In 2009-2013, also the relative economic level vis-à-vis the EA12 countries declined in the aforementioned economies, the largest drop (20 pp) being recorded in Greece. In contrast, the economic level relative to the EA12 average is increasing most quickly in the Baltic states. In the period of 2009-2013, it increased by 14 pp in Lithuania, by 11 pp in Latvia and by 7 pp in Estonia.

In the Czech Republic, the economic level measured by GDP per capita adjusted by current purchasing power parity was approximately 20,400 PPS in 2013, corresponding to 73% of economic level of the EA12. After a period of convergence in 2000-2007, when the Czech Republic's relative economic level vis-à-vis the EA12 countries increased by 13 pp, the Czech Republic has been stagnating since 2010. Due to the slow economic recovery, the relative economic level of the Czech Republic should stagnate in 2014 and could increase by 1 pp in 2015.

GDP per capita, when adjusted for the **exchange rate,** takes into account the market valuation of the currency and the ensuing differences in price levels. In the case of the Czech Republic, this indicator was approximately EUR 14,200 in 2013, i.e. 49% of the EA12 level. In the aforementioned year, the absolute and relative levels of GDP per capita adjusted for the exchange rate decreased, to which the CNB’s foreign exchange interventions also contributed. With regard to the assumption that the CNB will use the exchange rate as another monetary policy instrument until mid-2015, in 2014 we expect a further decrease in both absolute and relative levels.

When comparing price levels, the **comparative price level of GDP** in the Czech Republic decreased by 2 pp in 2013, thus reaching 67% of the EA12 average. The expected slight decrease in the comparative price level by a further 3 pp in 2014 should help maintain the Czech economy’s competitiveness.