

## Summary of the Forecast

According to the latest data, which are based on the national accounts standard ESA 2010 and reflect other methodical changes, real GDP increased by 0.3% QoQ in the second quarter of 2014. Compared with the first quarter of 2014, there was some slowdown of growth but this was in line with expectations. We, therefore, still hold the view that the economy should continue to grow at a moderate pace. Real GDP could increase by 2.4% YoY this year and maintain similar dynamics also in 2015. Growth in both years should be driven exclusively by domestic demand; the contribution of net exports should be close to zero.

Despite the weakening of the Czech koruna due to the CNB's foreign exchange interventions, the year 2014 should be characterized by very low inflation. Unlike in previous years, administrative measures (especially a decrease in electricity prices) should have an anti-inflationary impact throughout 2014. Average inflation rate could thus reach 0.5% this year. Consumer price growth should accelerate in 2015, but we assume that inflation will still be hovering below the CNB's inflation target.

Compared with the previous Macroeconomic Forecast, the forecast for labour market developments changed only little. Thanks to the gradual pick-up in economic

activity, the unemployment rate should be declining moderately, whereas employment should be modestly rising.

Total wage bill could increase by 2.9% this year. In 2015 we expect its growth to accelerate to 3.9%. A proposed increase in the wage bill in state administration, apart from an expected gradual improvement in the state of the private sector, should impact positively on total wage bill.

We expect the government sector to post a deficit of 1.5% of GDP this year. In absolute terms, the balance should slightly deteriorate compared with the last year, but the deficit will remain well below 3% of GDP. Owing to an improved liquidity management, the government sector debt should decrease by 1.8 pp to 43.9% of GDP. A deficit of 2.4% of GDP, given partially by a one-off inclusion of the lease of JAS 39 Gripen jet fighters, is expected for the next year.

Current account of the balance of payments should be balanced this year; in 2015 it could post a small deficit. Further increases of the balance of trade surplus will be compensated for by the continued deepening of the income balance deficits.

We regard risks to the Forecast as balanced.

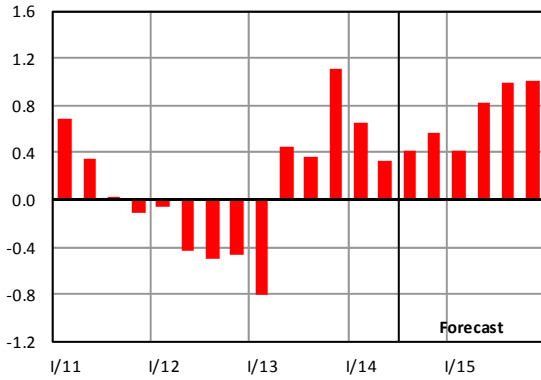
Table: **Main Macroeconomic Indicators**

		2010	2011	2012	2013	2014	2015	2013	2014	2015
		Current forecast					Previous forecast			
<b>Gross domestic product</b>	<i>bill. CZK</i>	<b>3 954</b>	<b>4 022</b>	<b>4 048</b>	<b>4 086</b>	<b>4 284</b>	<b>4 467</b>	3 884	4 061	4 216
<b>Gross domestic product</b>	<i>growth in %, const.pr.</i>	<b>2.3</b>	<b>2.0</b>	<b>-0.8</b>	<b>-0.7</b>	<b>2.4</b>	<b>2.5</b>	-0.9	2.7	2.5
<b>Consumption of households</b>	<i>growth in %, const.pr.</i>	<b>1.0</b>	<b>0.2</b>	<b>-1.8</b>	<b>0.4</b>	<b>1.4</b>	<b>1.7</b>	0.1	1.6	1.4
<b>Consumption of government</b>	<i>growth in %, const.pr.</i>	<b>0.4</b>	<b>-2.9</b>	<b>-1.0</b>	<b>2.3</b>	<b>1.9</b>	<b>2.0</b>	1.6	1.9	1.6
<b>Gross fixed capital formation</b>	<i>growth in %, const.pr.</i>	<b>1.3</b>	<b>1.1</b>	<b>-2.9</b>	<b>-4.4</b>	<b>4.5</b>	<b>4.9</b>	-3.5	4.1	3.5
<b>Contr. of foreign trade to GDP growth</b>	<i>p.p., const.pr.</i>	<b>0.5</b>	<b>1.9</b>	<b>1.3</b>	<b>0.0</b>	<b>-0.1</b>	<b>0.0</b>	-0.3	0.6	0.5
<b>Contr. of increase in stocks to GDP growth</b>	<i>p.p., const.pr.</i>	<b>0.8</b>	<b>0.2</b>	<b>-0.2</b>	<b>-0.2</b>	<b>0.4</b>	<b>0.0</b>	-0.2	0.0	0.2
<b>GDP deflator</b>	<i>growth in %</i>	<b>-1.5</b>	<b>-0.2</b>	<b>1.4</b>	<b>1.7</b>	<b>2.4</b>	<b>1.8</b>	1.9	1.8	1.3
<b>Average inflation rate</b>	<i>%</i>	<b>1.5</b>	<b>1.9</b>	<b>3.3</b>	<b>1.4</b>	<b>0.5</b>	<b>1.5</b>	1.4	0.6	1.7
<b>Employment (LFS)</b>	<i>growth in %</i>	<b>-1.0</b>	<b>0.4</b>	<b>0.4</b>	<b>1.0</b>	<b>0.4</b>	<b>0.3</b>	1.0	0.5	0.2
<b>Unemployment rate (LFS)</b>	<i>average in %</i>	<b>7.3</b>	<b>6.7</b>	<b>7.0</b>	<b>7.0</b>	<b>6.3</b>	<b>6.1</b>	7.0	6.4	6.1
<b>Wage bill (domestic concept)</b>	<i>growth in %, curr.pr.</i>	<b>0.6</b>	<b>2.2</b>	<b>2.1</b>	<b>-0.4</b>	<b>2.9</b>	<b>3.9</b>	-0.9	2.8	3.8
<b>Current account / GDP</b>	<i>%</i>	<b>-3.7</b>	<b>-2.6</b>	<b>-1.3</b>	<b>-1.4</b>	<b>0.0</b>	<b>-0.3</b>	-1.4	0.4	0.0
<b>Assumptions:</b>										
<b>Exchange rate CZK/EUR</b>		<b>25.3</b>	<b>24.6</b>	<b>25.1</b>	<b>26.0</b>	<b>27.5</b>	<b>27.5</b>	26.0	27.4	27.4
<b>Long-term interest rates</b>	<i>% p.a.</i>	<b>3.7</b>	<b>3.7</b>	<b>2.8</b>	<b>2.1</b>	<b>1.7</b>	<b>1.7</b>	2.1	1.9	2.4
<b>Crude oil Brent</b>	<i>USD/barrel</i>	<b>80</b>	<b>111</b>	<b>112</b>	<b>109</b>	<b>105</b>	<b>101</b>	109	108	104
<b>GDP in Eurozone (EA-12)</b>	<i>growth in %, const.pr.</i>	<b>1.9</b>	<b>1.6</b>	<b>-0.6</b>	<b>-0.4</b>	<b>0.7</b>	<b>1.1</b>	-0.4	1.1	1.6

Source: CNB, CZSO, Eurostat, U. S. Energy Information Administration, own calculations

### Economic recovery should continue

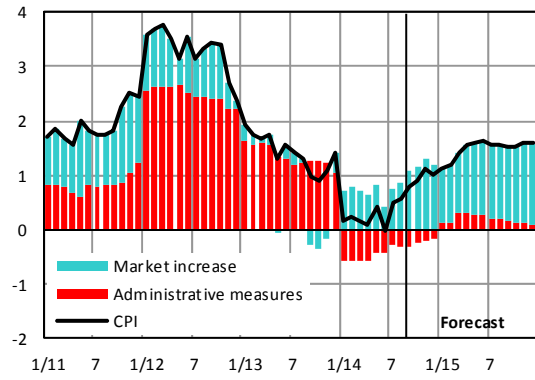
real GDP, QoQ growth rate, in %, seasonally adjusted



Source: CZSO, own calculations

### Inflation gradually approaching the inflation target

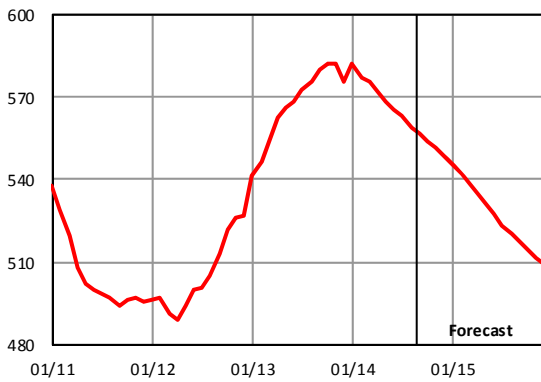
decomposition of YoY growth of CPI, contributions in pp



Source: CZSO, own calculations

### Unemployment should continue to decline

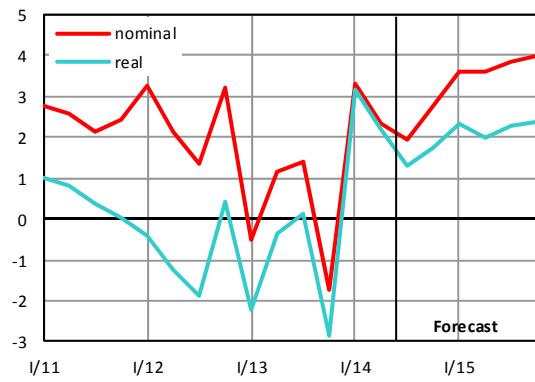
registered unemployment, in thousands of persons, seasonally adjusted



Source: Ministry of Labour and Social Affairs, own calculations

### Moderate growth of average real wage

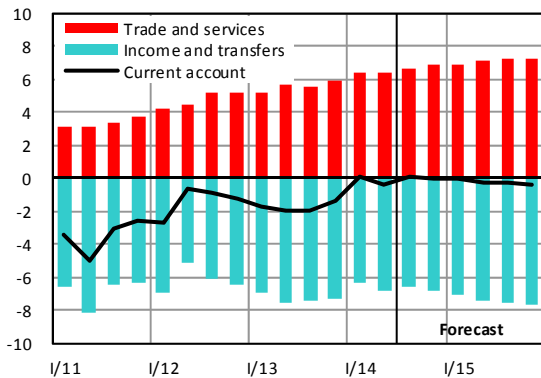
YoY growth rate, in %



Source: CZSO, own calculations

### Current account almost balanced

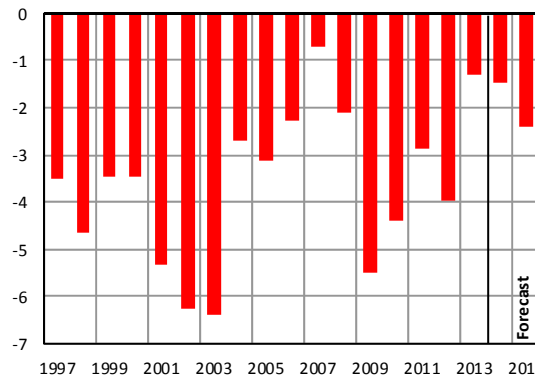
in % of GDP (moving sums of the latest 4 quarters)



Source: CNB, CZSO, own calculations

### General government deficit under 3% of GDP

general government balance, in % of GDP



Source: CZSO, own calculations