

# **Macroeconomic Forecast of the Czech Republic**

**April 2018**

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ISSN 2533-5588

Issued quarterly, free distribution

Electronic archive:  
<http://www.mfcz.cz/macroforecast>

# **Macroeconomic Forecast**

## **of the Czech Republic**

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The Macroeconomic Forecast is prepared by the Economic Policy Department of the Czech Ministry of Finance. It contains a forecast for the current and the following year (i.e. until 2019) and for certain indicators an outlook for another 2 years (i.e. until 2021). It is published on a quarterly basis (usually in January, April, July and November) and is also available on the website of the Ministry of Finance at:

***[www.mfcr.cz/macroforecast](http://www.mfcr.cz/macroforecast)***

Any comments or suggestions that would help us improve the quality of our publication and closer satisfy the needs of its users are welcome. Please send any comments to the following email address:

***[macroeconomic.forecast@mfcr.cz](mailto:macroeconomic.forecast@mfcr.cz)***

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## List of Abbreviations

BoP.....	balance of payments
const.pr.....	constant prices
CNB.....	Czech National Bank
CPI.....	consumer price index
CR.....	Czech Republic
curr.pr.....	current prices
CZSO.....	Czech Statistical Office
EA19.....	euro zone consisting of 19 countries
EC.....	European Commission
ECB.....	European Central Bank
ESI.....	Economic Sentiment Indicator
EU28.....	European Union consisting of 28 countries
Fed.....	Federal Reserve System
GDP.....	gross domestic product
GVA.....	gross value added
IMF.....	International Monetary Fund
LFS.....	Labour Force Survey
MoF.....	Ministry of Finance
pp.....	percentage points
rev.....	revisions
TFP.....	total factor productivity
VAT.....	value added tax

## Basic Terms

Prelim. (preliminary data)	data from quarterly national accounts, released by the CZSO, as yet unverified by annual national accounts
Estimate	data for past period that were unavailable as of the cut-off date
Forecast	forecast of future numbers, using expert and mathematical methods
Outlook	projection of more distant future numbers, using mainly extrapolation methods

## Symbols Used in Tables

-	A dash in place of a number indicates that the phenomenon did not occur.
.	A dot in place of a number indicates that we do not forecast that variable, or the figure is unavailable or unreliable.
x, (space)	A cross or space in place of a number indicates that no entry is possible for logical reasons.

## Cut-off Date for Data Sources

The forecast was made on the basis of data known as of **3 April 2018**.

## Notes

All data in the Macroeconomic Forecast are unadjusted for seasonal and calendar effects, unless stated otherwise. Published aggregate data may not match sums of individual items to the last decimal place due to rounding.

Data from the previous forecast (January 2018) are indicated by italics. Data relating to the years 2020 and 2021 are an extrapolation scenario that indicates only the direction of possible developments, and as such are not commented upon in the following text.

# Summary of the Forecast

The growth of the world economy remains strong. It is supported by investment, dynamics of the global trade, favourable financial conditions and expansive economic policies. In 2017 the economic growth in both the Euro Area and the European Union significantly exceeded previous expectations, confirming the transition from recovery to economic expansion. Favourable developments are expected also in this and the next year. The continued growth should be accompanied by an improvement in the labour market situation, unprecedentedly high confidence of economic entities and the resulting increase in household consumption and revival of investment activity.

The favourable developments in countries of the main trading partners and the positive situation within the Czech economy create conditions for further successful continuation of the economic boom in the Czech Republic. The main barrier for a higher growth can be considered the situation in the labour market, which shows symptoms of overheating.

The YoY real **gross domestic product** growth **accelerated to 5.5%** in the fourth quarter of 2017, which is the most since the second quarter 2015, when the economy was, however, largely stimulated by the end of the 2007–2013 financial perspective of European Union projects. In the QoQ comparison (after adjustment for seasonal and calendar effects), the economic growth accelerated slightly to **0.8%**.

A traditionally significant component of use was **household consumption**. It increased by 4.3% YoY, not only due to high dynamics of the wage bill, but also due to a decrease in the savings rate, which reflects situation in the labour market, low interest rates and high consumer confidence in future developments. The general government consumption growth was 1.5%.

The growth in **investment in fixed capital** continued to accelerate in the fourth quarter, to 7.8%. Investment in machinery, equipment (excluding transport equipment) and information and communication technologies accounted for almost a half of that result. However, growth was recorded in all categories of investment. In sectoral terms, the high investment activity was driven by private investment as well as investment of the general government sector. Gross capital formation (including change in inventories) recorded even double-digit growth (11.5%).

In the fourth quarter of 2017, the contribution of **foreign trade** with goods and services to the economic growth was only slightly positive (0.1 pp). Growth in exports, supported by increasing external demand, thus almost offset the growth in imports, which reflected mainly a high import intensity of exports and investments.

The positive economic situation should continue also in **2018 and 2019**. Growth should continue to be driven by household consumption reflecting the wage dynamics and an extremely low unemployment rate, an increasing participation rate and a very high number of job vacancies. Investment should be stimulated not only by funds from the European Structural and Investment Funds, a need of the private sector to innovate technological equipment amid imbalances in the labour market but also by decreasing relative cost of capital to the cost of labour at still low real interest rates.

**Real gross domestic product growth in 2017** reached **4.4%**. **The forecast for 2018** is revised slightly upwards from 3.4% to **3.6%**. Due to an increased likelihood that similarly favourable economic developments will continue also in the next year, the forecast for GDP growth in **2019** is **raised** more significantly from 2.6% to **3.3%**. There is also a change in the expected growth structure for both years—the dynamics of domestic demand increases, which is offset by a lower contribution of net exports to GDP growth.

Since the beginning of 2017, the YoY **consumer prices** growth oscillates, with a few exceptions, in the upper half of the tolerance band of the Czech National Bank's 2% inflation target. We expect, however, that anti-inflationary effects resulting from the anticipated tightening of monetary conditions, especially in the exchange rate component, will outweigh pro-inflationary effects of rising wages and a positive output gap. Therefore, we are lowering the forecast for the average **inflation rate** in 2018 and 2019, also with regard to an error in the January forecast, from 2.6% to 2.1% and from 2.1% to 1.9%, respectively.

High employment growth, which has steadily exceeded 1% since the end of 2014, has almost exhausted unused resources in the **labour market**. Lack of employees is thus becoming a barrier for an extensive production growth, which motivates companies for investment increasing labour productivity.

The room for a further decline in unemployment is, apparently, very limited. We thus keep the forecast for the **unemployment rate** in 2018 and 2019 at 2.4% and 2.3%, respectively.

The **current account of the balance of payments** reached a surplus of 1.1% of GDP in 2017. The positive balances of goods and services significantly exceed the deficit of primary income, which is mostly influenced by an outflow of income from foreign direct investment in the form of dividends and reinvested earnings. The surplus on the current account was lower in 2017 than for most of 2016, mainly due to higher domestic demand for imports influenced by the growth in consumption and investment.

With regard to the current revision of data for 2016 and 2017 (higher current account surplus) and the changes in expected structure of economic growth outlined above, the forecast for the **current account surplus** increases slightly to 0.4% of GDP in 2018 and 0.2% of GDP in 2019.

The **balance of the general government sector** reached a record-high surplus of 1.6% of GDP in 2017. It also resulted in a YoY improvement of 0.2 pp in the structural balance, which reached a surplus of 1.1% of GDP. The

improved budget performance of the general government sector was significantly driven by revenues of public budgets, as tax revenues – including social security contributions – rose by 7.7%. The level of total indebtedness also reflects the record-high surplus, having decreased by 2.2 pp YoY to 34.6% of GDP. For the year 2018 the forecast envisages a positive balance amounting to 1.5% of GDP and further decrease in debt to the level of 32.9% of GDP.

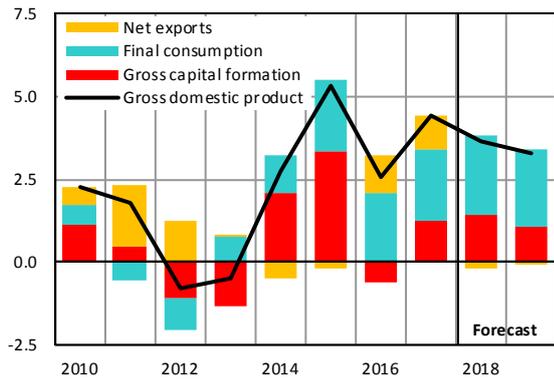
**Table: Main Macroeconomic Indicators**

		2013	2014	2015	2016	2017	2018	2019	2017	2018	2019
		Current forecast							Previous forecast		
<b>Gross domestic product</b>	<i>bill. CZK</i>	<b>4 098</b>	<b>4 314</b>	<b>4 596</b>	<b>4 773</b>	<b>5 055</b>	<b>5 320</b>	<b>5 596</b>	5 042	5 304	5 530
<b>Gross domestic product</b>	<i>real growth in %</i>	<b>-0.5</b>	<b>2.7</b>	<b>5.3</b>	<b>2.6</b>	<b>4.4</b>	<b>3.6</b>	<b>3.3</b>	4.3	3.4	2.6
<b>Consumption of households</b>	<i>real growth in %</i>	<b>0.5</b>	<b>1.8</b>	<b>3.7</b>	<b>3.6</b>	<b>4.0</b>	<b>4.3</b>	<b>4.1</b>	4.0	3.7	2.7
<b>Consumption of government</b>	<i>real growth in %</i>	<b>2.5</b>	<b>1.1</b>	<b>1.9</b>	<b>2.0</b>	<b>1.5</b>	<b>1.9</b>	<b>2.0</b>	1.9	1.8	1.5
<b>Gross fixed capital formation</b>	<i>real growth in %</i>	<b>-2.5</b>	<b>3.9</b>	<b>10.2</b>	<b>-2.3</b>	<b>5.4</b>	<b>5.7</b>	<b>4.4</b>	5.6	4.1	3.4
<b>Net exports</b>	<i>contr. to GDP growth, pp</i>	<b>0.1</b>	<b>-0.5</b>	<b>-0.2</b>	<b>1.2</b>	<b>1.0</b>	<b>-0.2</b>	<b>-0.1</b>	1.0	0.2	0.1
<b>Change in inventories</b>	<i>contr. to GDP growth, pp</i>	<b>-0.7</b>	<b>1.1</b>	<b>0.8</b>	<b>0.0</b>	<b>-0.1</b>	<b>0.0</b>	<b>0.0</b>	-0.3	0.0	0.0
<b>GDP deflator</b>	<i>growth in %</i>	<b>1.4</b>	<b>2.5</b>	<b>1.2</b>	<b>1.2</b>	<b>1.4</b>	<b>1.5</b>	<b>1.8</b>	1.3	1.8	1.7
<b>Average inflation rate</b>	<i>%</i>	<b>1.4</b>	<b>0.4</b>	<b>0.3</b>	<b>0.7</b>	<b>2.5</b>	<b>2.1</b>	<b>1.9</b>	2.5	2.6	2.1
<b>Employment (LFS)</b>	<i>growth in %</i>	<b>1.0</b>	<b>0.8</b>	<b>1.4</b>	<b>1.9</b>	<b>1.6</b>	<b>0.7</b>	<b>0.2</b>	1.6	0.6	0.2
<b>Unemployment rate (LFS)</b>	<i>average in %</i>	<b>7.0</b>	<b>6.1</b>	<b>5.1</b>	<b>4.0</b>	<b>2.9</b>	<b>2.4</b>	<b>2.3</b>	2.9	2.4	2.3
<b>Wage bill (domestic concept)</b>	<i>growth in %</i>	<b>0.5</b>	<b>3.6</b>	<b>4.8</b>	<b>5.8</b>	<b>8.3</b>	<b>7.7</b>	<b>6.5</b>	7.9	7.7	4.9
<b>Current account balance</b>	<i>% of GDP</i>	<b>-0.5</b>	<b>0.2</b>	<b>0.2</b>	<b>1.6</b>	<b>1.1</b>	<b>0.4</b>	<b>0.2</b>	0.5	0.1	0.1
<b>General government balance</b>	<i>% of GDP</i>	<b>-1.2</b>	<b>-2.1</b>	<b>-0.6</b>	<b>0.7</b>	<b>1.6</b>	<b>1.5</b>	<b>1.1</b>	1.1	1.3	.
<b>Assumptions:</b>											
<b>Exchange rate CZK/EUR</b>		<b>26.0</b>	<b>27.5</b>	<b>27.3</b>	<b>27.0</b>	<b>26.3</b>	<b>25.1</b>	<b>24.7</b>	26.3	25.4	25.0
<b>Long-term interest rates</b>	<i>% p.a.</i>	<b>2.1</b>	<b>1.6</b>	<b>0.6</b>	<b>0.4</b>	<b>1.0</b>	<b>1.9</b>	<b>2.2</b>	1.0	1.7	2.0
<b>Crude oil Brent</b>	<i>USD/barrel</i>	<b>109</b>	<b>99</b>	<b>52</b>	<b>44</b>	<b>54</b>	<b>65</b>	<b>61</b>	54	68	64
<b>GDP in Eurozone</b>	<i>real growth in %</i>	<b>-0.2</b>	<b>1.3</b>	<b>2.1</b>	<b>1.8</b>	<b>2.3</b>	<b>2.3</b>	<b>1.8</b>	2.4	2.3	1.9

Source: CNB, CZSO, Eurostat, U. S. Energy Information Administration. Calculations of the MoF.

### Domestic demand should be the main driver of growth

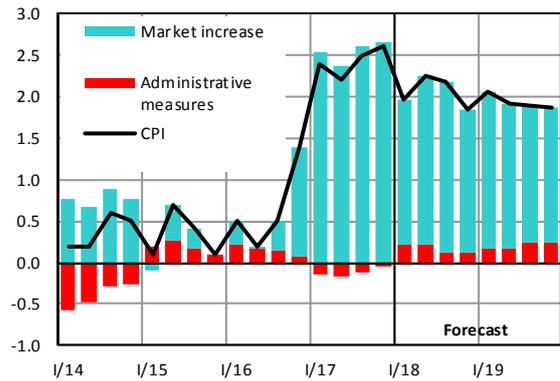
YoY growth rate of real GDP in %, contributions of individual expenditure components in percentage points



Source: CZSO. Calculations of the MoF.

### Inflation should hover close to the 2% target of the CNB

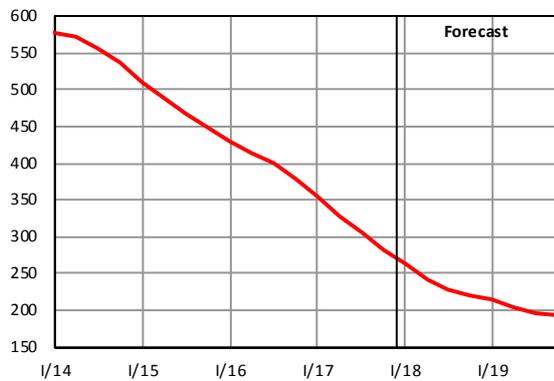
decomposition of YoY growth of CPI, contributions in pp



Source: CZSO. Calculations of the MoF.

### Unemployment should continue to decline further

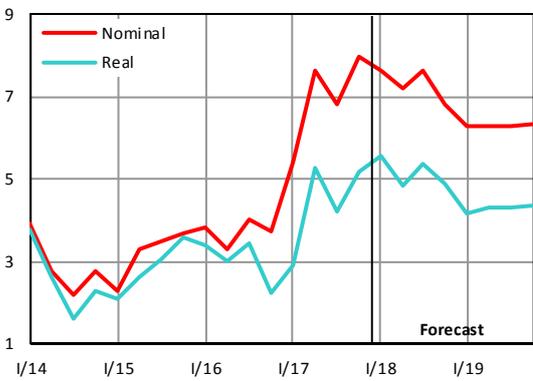
registered unemployment, in thous. of persons, seasonally adjusted



Source: Ministry of Labour and Social Affairs. Calculations of the MoF.

### Dynamic growth of wages should continue

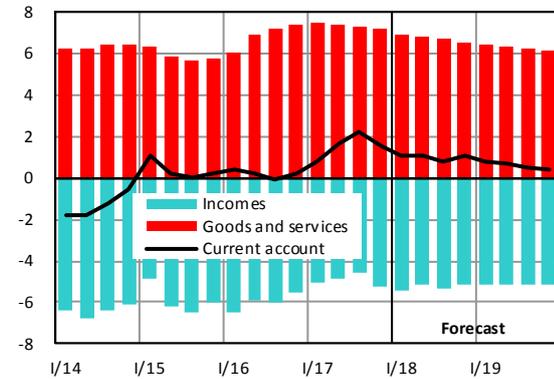
average gross monthly wage, YoY growth rate, in %



Source: CZSO. Calculations of the MoF.

### Current account should remain in moderate surplus

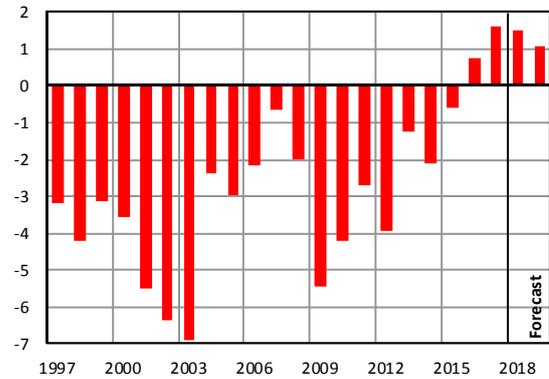
in % of GDP (yearly moving sums)



Source: CNB, CZSO. Calculations of the MoF.

### Balance of the general government should stay positive

in % of GDP



Source: CZSO. Calculations of the MoF.

## Forecast Risks and Uncertainty

The Macroeconomic Forecast is subject to a number of positive and negative risks. If we take into account the likelihood of their fulfilment, we consider the **forecast risks tilted slightly to the downside**.

Prospects of economies of our main trading partners continue to improve. In the Euro Area as a whole as well as in largest economies of the monetary union, a number of “soft indicators” hover close to historical or at least multi-year highs. The economic development in the Euro Area could thus be even more favourable than expected, which would considerably benefit the strongly export-oriented Czech economy. Besides the **growth in foreign demand**, the Czech economy could be influenced through foreign trade also negatively. Risks in this respect include, first, trends towards an increase in **protectionism** (the CR does trade mostly with other EU countries, but indirect exposure to some non-EU countries need not be negligible), and, second, the form of the future **arrangement of relations between the United Kingdom and the EU** in the area of free movement of goods and services. However, given the information available and the progress made in negotiations, any increase in the barriers to foreign trade with the United Kingdom would impact the Czech economy only at the end of the outlook horizon. We continue to expect that both parties to the negotiations will be interested in mitigating the impacts of the United Kingdom’s withdrawal from the EU as much as possible. Furthermore, the Czech economy could be adversely influenced by an escalation of problems of the Italian banking sector as well as geopolitical factors.

The Czech economy is showing marked signs of overheating in some areas, especially in the labour market. In terms of **cyclical development of the economy**, one cannot rule out the possibility of the economy entering the downward phase of the business cycle in the forecast horizon, should some risks listed here materialize. The lack of adequately qualified employees is increasingly seen by companies as a barrier to raising their production. A key factor for the continuation of the economic growth, especially in the medium and longer horizons, will be the increase in **labour productivity**, considering

the current labour market situation and anticipated demographic developments. However, labour productivity could fall behind expectations due e.g. to lower investment dynamics, which would negatively affect the pace of economic growth. In the short term, imbalances in the labour market create a **strong pressure on wage growth**, which results in increased unit labour costs. If that lasted for long, the competitiveness of some companies could be negatively affected, but on the other hand this factor significantly supports the growth in disposable income of households and in investment increasing labour efficiency, creating a stimulus for greater orientation on the production of goods and services with higher value added.

**Considered changes in the area of personal income tax** constitute uncertainty in terms of the forecast for household consumption and economic growth. In the case of **investment**, the recovery of the investment cycle linked to the EU programming period 2014–2020 will be crucial. In the longer term, the gap due to the discontinuation of the United Kingdom’s payment to the EU budget will be significant, as well as the new allocation associated with the higher relative development level of the regions of the Czech Republic and possible redirection of funds in the EU budget to other priorities.

The cyclical development of the economy in connection with low interest rates led to an increased dynamics of mortgage loans. Together with the factors limiting the supply of residential real estate (some of which are Prague-specific), this development has contributed to a significant growth in offer prices of flats. Continuing **rapid growth in housing loans and property prices** could pose macroeconomic risks in the future as some households might not be able to repay their loans in the case of worsening economic situation or an increase in market rates, which would also have an impact on financial stability. The dynamics of housing loans, however, declined slightly in comparison with mid-2017 in connection with an increase in interest rates and the achieved high level of flat prices. The data on residential construction and issued building permits suggests that the supply of residential real estate should increase in the future.

# 1 Forecast Assumptions

## 1.1 External Environment

In the fourth quarter of 2017, GDP growth in the USA and Western Europe slowed down slightly. Dynamics of the Chinese economy also decreased moderately but they still remain high as they are largely supported by fiscal stimuli. A number of other large emerging economies succeeded in overcoming recession and returned to the trajectory of economic growth. The global economic growth remains strong, and the cyclical upswing of the world economy should continue.

### 1.1.1 United States of America

In the fourth quarter of 2017, growth of the US economy slowed down marginally, with GDP increasing by 0.7% QoQ (*in line with the estimate*). Economic growth was driven exclusively by domestic demand, especially accelerating household consumption expenditures and investments. The increased household consumption was mainly due to good labour market situation and consumer confidence (the highest since 2004), and the main contributors to gross fixed capital formation were investments in transport equipment and residential real estate. Government consumption expenditure increased only slightly, while the contribution of a change in inventories weighed on economic growth, similarly to the balance of foreign trade. Due to the strong domestic demand, the growth rate of imports outpaced the growth rate of exports, which was dampened by a decrease in exports of services.

At its March meeting the Fed raised the interest rates further by 0.25 pp to 1.50–1.75% in relation to the growth in the number of vacancies, low unemployment rate and the inflation outlook. At the same time it announced that it plans to increase the rates two more times during 2018 and three times in the next year, depending on economic developments. In October 2017 the Fed started selling assets worth USD 10 billion monthly. The monthly volume of sold assets doubled in January, and it will be increased by further USD 10 billion every three months during 2018 to a total, for the time being, of USD 50 billion. The inflation rate started to grow slightly again in July 2017, reaching 2.2% in February. However, the Fed expects the inflation rate to stabilize around the 2% target in the medium term.

We expect that the economy will maintain its growth rate also in the coming years, and that household consumption will remain the key factor. Private consumption is supported by high consumer confidence and good situation in the labour market, where the unemployment rate was only 4.1% in January, the lowest value since December 2000. There is already a shortage of labour force in the labour market; however, a more dynamic wage growth is still hampered by a relatively high

number of involuntary part-time workers or a low employment rate, which has not yet reached the pre-crisis level. Household consumption and corporate investments should also be boosted by the approved tax reform, which increased tax deductions and tax rebate for a child for natural persons, and dramatically reduced the income tax rate from 35% to 21% for legal entities. The economy should also benefit from infrastructure investments; however, no details on the amount and timing of this fiscal stimulus are known, for the time being. The main stock index Dow Jones, which reached its historic maximum in January, recorded a slight correction in the following month reflecting investor concerns about interest rate hikes. Economic growth reached 2.3% in 2017 (*in line with the estimate*). For 2018, we expect GDP growth at 2.7% (*versus 2.6%*), and for 2019 at 2.2% (*unchanged*).

### 1.1.2 China

The performance of the Chinese economy maintains its dynamics. The QoQ GDP growth was solid at 1.6% in the fourth quarter of 2017, and the GDP growth for the entire 2017 slightly accelerated to 6.9%. China thus remains the main driver of the global economic growth. Services are becoming the dominant sector, while the importance of industry is getting weaker. The core of economic growth has also been gradually shifting from investments and exports to household consumption, as evidenced by a dynamic growth in retail sales and imports of goods. Growth in investments is also gradually slowing down as a result of a number of measures, whereby the government attempts to limit rising prices of housing and higher-risk loans or to reduce the overcapacity in some industries through stricter environmental regulations.

We expect that the rate of economic growth will slow down very gradually in the coming years. The development of leading indicators remains promising, particularly the development of consumer confidence, which has reached the highest values since 1993. The situation in financial markets is stabilized and foreign exchange reserves have been slowly growing since the turn of 2016 and 2017. However, the levels and dynamics of the general government and private sector debts and the share of non-performing loans cause major concerns as they could threaten the stability of the economy in the case of a major slowdown in economic growth. From the long-term perspective, a major risk is mainly the unfavourable demographic development.

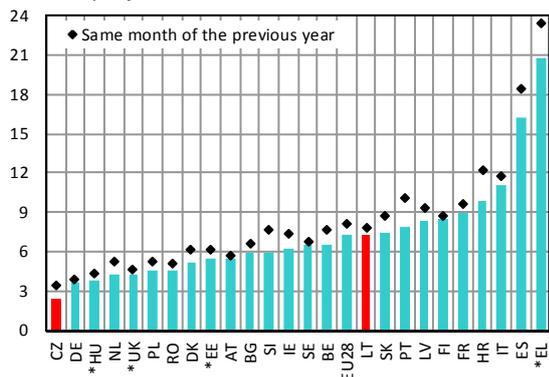
### 1.1.3 European Union

Despite a slight slowdown at the end of 2017, the economic growth in the European Union remains the strongest since 2011. The QoQ GDP growth in the fourth quarter of 2017 was 0.6% both in the EU28 and the EA19 (in both cases in line with the estimate). In YoY terms, GDP increased by 2.6% in the EU28 and by 2.7% in the EA19 (in both cases in line with the estimate). Economic growth was recorded in all EU28 economies except Malta and Luxembourg; however, marked differences remain among individual countries. In a number of these economies a more significant recovery is still being hampered by structural problems, loss of competitiveness or high indebtedness of the government and private sectors.

Since the beginning of 2017, the price level growth in the EA19 has been slowing down slightly, with the inflation rate in the EA19 reaching only 1.1% in February. The ECB has been keeping the main refinancing rate at 0.00% and the deposit rate at -0.40% already since March 2016. It also assumes that benchmark interest rates remain at the current or lower levels for a long time, definitely beyond the horizon of net asset purchases. Monthly purchases of assets worth 30 billion EUR should take place until September 2018, or even longer if necessary, and in any case until the Governing Council sees a sustainable correction of the inflation development in line with its inflation target. The aim of the eased monetary conditions is to increase credit activity and ensure that inflation, through an increase in investment and consumption, returns to the inflation target (inflation below, but close to, 2%).

#### Graph 1.1.1: Unemployment rate in the EU in January 2018

in%, seasonally adjusted data, LFS



Note: \*) December 2017.  
Source: Eurostat.

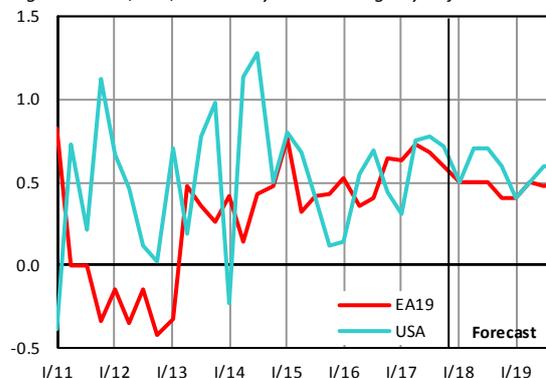
Related to the economic recovery, the labour market situation has also been improving gradually; however, many countries lack qualified workers. The unemployment rate in the EU28 has been decreasing since mid-2013, reaching 7.3% in January 2018 (YoY decrease of 0.8 pp). However, enormous differences still persist among individual economies. The worst situation continues to be in Greece, where the unemployment rate

stood at 20.8% in December 2017. In the EU28 countries for which data for January was available as of the cut-off date, the unemployment rate exceeded 10% in Spain (16.3%) and Italy (11.1%) Conversely, the lowest rates were recorded in the Czech Republic (2.4%), Malta (3.5%) and Germany (3.6%).

The excellent condition of the Euro Area is also testified by the so-called “soft indicators”, many of which exceeded their historical or at least multi-year highs at the turn of 2017 and 2018. In December 2017, the business climate indicator (monitored since 1985), and the Manufacturing Purchasing Managers Index (monitored since 1997) reached their historical highs. The Services Purchasing Managers Index is also developing favourably, reaching its ten-year high in January. Consumer confidence in the Euro Area was the highest since 2000 in January.

#### Graph 1.1.2: Growth of GDP in the EA19 and in the USA

QoQ growth rate, in%, seasonally and working day adjusted



Source: Eurostat. Calculations of the MoF.

We expect economic growth to be driven mainly by domestic demand also in the coming years. Household consumption will remain the main driver of the economy’s growth, supported by low interest rates in the short term. The improving labour market situation, and a related gradual increase in the wage growth rate, will have more permanent effects. Investments, which will continue to be supported by the eased monetary policy of the ECB, will be negatively affected by the uncertainty associated with the United Kingdom’s decision to withdraw from the EU as the future set-up of the EU–UK trade relationships has not yet been agreed. However, the United Kingdom should have access to the EU single market and remain in the customs union until the end of 2020. The economic growth in the Euro Area will probably continue to be hampered by persisting problems in the banking sector in the Euro Area or high indebtedness of some economies. In the context of gradual acceleration of global growth, exports should also slightly gain dynamics; however, a significant negative risk in this respect is a possible re-introduction of import tariffs by the USA on cars, and opening of a trade war. Real GDP growth in the Euro Area was 2.3% in 2017 (versus 2.4%). We expect the EA19 economy to grow at the same pace

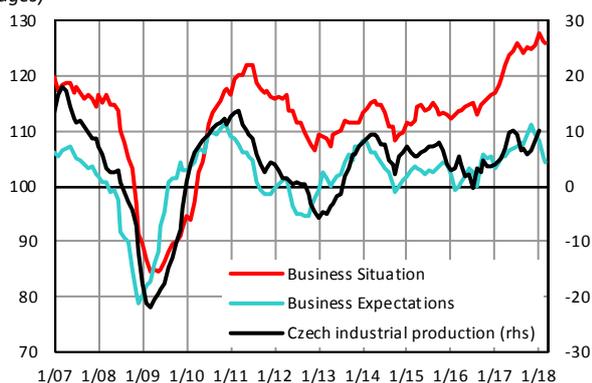
also in 2018 (*unchanged*) and the growth to slow down to 1.8% in 2019 (*versus 1.9%*).

The QoQ growth of the **German** economy recorded a mild slowdown to 0.6% (*in line with the estimate*) in the fourth quarter of 2017. The GDP was driven by foreign demand as the German economy fully benefits from the global economic growth. Household consumption expenditures stagnated despite a good labour market situation, wage growth and a high level of consumer confidence. The gross fixed capital formation growth also stagnated as the growth rate of investments in machinery and equipment slowed down, and construction investments recorded a decline for the second consecutive quarter. The only growing component of domestic demand was government consumption.

The labour market situation can be considered strained because the German economy is close to full employment. In January, the unemployment rate remained at 3.6%, and employment and the number of job vacancies reached the highest values since German reunification. Although shortage of employees has been increasingly evident in the labour market, the wage growth remains moderate. Soft indicators have been developing favourably. In January, business confidence measured by the Ifo index recorded the highest level since 1991, i.e. since the indicator has been monitored. The Manufacturing Purchasing Managers Index then reached its historically highest value since 1996 in December 2017. Last but not least, the development of the Consumer Confidence Index (GfK), which reached its highest value since 2001 in February, has been very promising.

### Graph 1.1.3: Ifo (Germany) and Czech manufacturing production

2005=100 (Ifo), seasonally adjusted index of industrial production in the Czech manufacturing, YoY growth in% (from quarterly moving averages)



Source: CESifo, CZSO.

We expect that economic growth will continue to be driven by both domestic and foreign demand also in the coming years. Household consumption expenditures will be supported mainly by the good labour market situation and related real wage growth resulting from the shortage of adequately skilled workers. A more dynamic growth in business investments can be expected due to

relatively high capacity utilization. Corporate investments and exports will be positively influenced by acceleration of global activity or reduction in political uncertainty because a coalition agreement was signed in March, six months after the parliamentary elections. However, the United Kingdom's withdrawal from the EU could be a risk factor, as the UK's share in the total exports in 2016 was 8.0% (3.7% of the German GDP). The economic growth was 2.2% in 2017 (*versus 2.4%*). The GDP could increase by 2.4% (*unchanged*) in 2018 and by 2.1% (*unchanged*) in 2019.

The QoQ growth of the **French** economy slightly accelerated to 0.6% (*versus 0.5%*) in the fourth quarter of 2017. The economic growth has been driven by foreign demand, with the growth rate of exports exceeding the growth rate of imports as a result of a strong demand for transport equipment. Domestic demand had a neutral effect on the economic growth as the growth in investments and consumption was offset by a negative contribution of the change in inventories. The growth of gross fixed capital formation was mainly due to increased investments in construction, transport and information and communication activities. The growth in household consumption expenditures slowed down mainly due to a decrease in expenditures on goods and energy.

The labour market situation has started improving very slowly. In January, the unemployment rate declined to 9.0% (a YoY decline by 0.7 pp), and a reform of the Labour Code could help make the labour market more flexible. In the short term, soft indicators point to some improvement in economic developments, many of them showing an upward trend. In January, the business confidence indicator reached the highest value in the past 17 years. The Manufacturing and Services Purchasing Managers Indexes still indicate a solid economic performance despite a slight decline in the past months. Economic growth should also be supported by a gradual reduction in the corporate income tax or adjustments to the taxation of capital income. A higher economic performance, however, will be hampered by long-term problems of the French economy – low competitiveness and the associated declining share in export markets or high and ever increasing government and private sector debts. GDP growth reached 1.8% in 2017 (*in line with the estimate*). We expect that the performance of the French economy will slightly fall behind the performance of the EA19 also in the following years, and the economic growth will thus reach 2.1% in 2018 (*versus 1.9%*) and 1.7% (*versus 1.6%*) in 2019.

The QoQ growth of the **Polish** economy slowed down slightly to 1.0% (*versus 0.9%*) in the fourth quarter of 2017. The solid performance was due to domestic demand only, especially household consumption expenditures supported by employment growth, accelerating wage growth and a high consumer confidence. The recovery of gross fixed capital formation was mainly due to the government sector investments in connection with

the start of the 2014–2020 financial perspective. Conversely, the balance of foreign trade dampened GDP growth as the growth rate of imports with regard to the accelerating domestic demand significantly exceeded the dynamics of exports. Economic growth should be driven mainly by household consumption also in the coming years, although its rate will gradually slow down. In the short term, it will be supported by low interest rates and high consumer confidence, which reached the highest value in the recorded history since 2000 in January and February. In the long term, there will be a significant impact of wage growth associated with the good labour market situation, where the unemployment rate was only 4.5% in January. Investment growth should gradually accelerate with the start of programmes in the 2014–2020 financial perspective and a need for capital renewal, however, lower predictability of government policies is a risk and in terms of long-term sustainability of the government finances a substantial risk results also from the abrupt decrease in the statutory retirement age. Real GDP increased by 4.6% in 2017 (*versus 4.4%*). We expect that economic growth should gradually slow down to 3.9% (*versus 3.6%*) in 2018 and to 3.4% (*versus 3.3%*) in 2019.

The **Slovak** economy recorded a QoQ growth of 0.9% (*versus 0.8%*) in the fourth quarter of 2017, driven exclusively by foreign demand. While exports and imports of goods increased, exports and imports of services decreased. Domestic demand hampered growth as weak growth in household and government consumption expenditures could not offset a fall in the gross capital formation caused by a decrease in investments and primarily by a negative contribution of the change in inventories. Similarly to 2017, domestic demand should remain the driver of economic growth also in the coming years. Household consumption will be supported by high level of consumer confidence, low interest rates and, most importantly, the still improving labour market situation. The unemployment rate was 7.5% in January 2018 (YoY decline of 1.2 pp), which is the lowest value in the recorded history since 1998. The labour market mismatch between supply and demand has been creating pressure on wage growth, the YoY growth of which was 5.2% in the fourth quarter. An increase in the minimum wage by 10.3% and growing salaries in the public administration will contribute to disposable income growth in 2018. A recovery of investment activity will be supported by continued investments in the automotive industry or government investments in infrastructure. Start of production of the Volkswagen and Jaguar Land Rover car factories should significantly contribute to an acceleration of exports in 2018 and 2019. Economic growth will also be supported by a reduction in the tax burden of companies and entrepreneurs. However, an

unstable political situation or high dependence on the automotive industry represent a negative risk. GDP growth reached 3.4% in 2017 (*in line with the estimate*). The economic growth in the coming years should gradually accelerate, to 3.7% (*unchanged*) in 2018 and 3.9% (*unchanged*) in 2019.

#### 1.1.4 Commodity Prices

We estimate that the average price of Brent crude oil reached USD 67/barrel (*versus USD 70/barrel*) in the first quarter of 2018. It thus increased by 8% QoQ and even 24% YoY. At the end of January 2018, the price climbed above USD 70/barrel, but it fell subsequently in connection with a correction in financial markets.

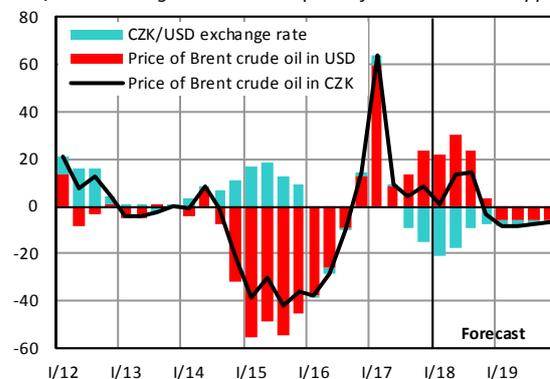
The agreement of the Organization of the Petroleum Exporting Countries and some other states to limit production has so far been successfully adhered to, which is, together with an increasing demand for crude oil driven by the global economic growth, a fundamental factor behind the rise in crude oil prices. On the supply side, an increase in production in the United States of America acts against the curbed production of the OPEC countries. This year the USA could become the main crude oil producer in the world, according to some estimates.

Further projected development in Brent crude oil price reflects the declining curve of the futures prices. The average price should reach USD 65/barrel in 2018 (*versus USD 68/barrel*), and we expect a slightly lower average price of USD 61/barrel in 2019 (*versus USD 64/barrel*). The downward change in the forecast is due to a decrease in the curve of futures prices in all delivery dates.

In koruna terms, the forecast for the Brent oil price dropped more, compared to the previous forecast, than the dollar price as we expect the koruna to be stronger against the dollar. According to our estimates, the koruna crude oil price should increase by approx. 6% in 2018, though it should decrease by almost 8% in 2019 (see also Graph 1.1.4).

#### Graph 1.1.4: Koruna Price of Brent Crude Oil

YoY change of the koruna price of Brent crude oil in %, contributions of the CZK/USD exchange rate and USD price of Brent crude oil in pp



Source: CNB, U. S. Energy Inf. Administration. Calculations of the MoF.

**Table 1.1.1: Gross Domestic Product – yearly**

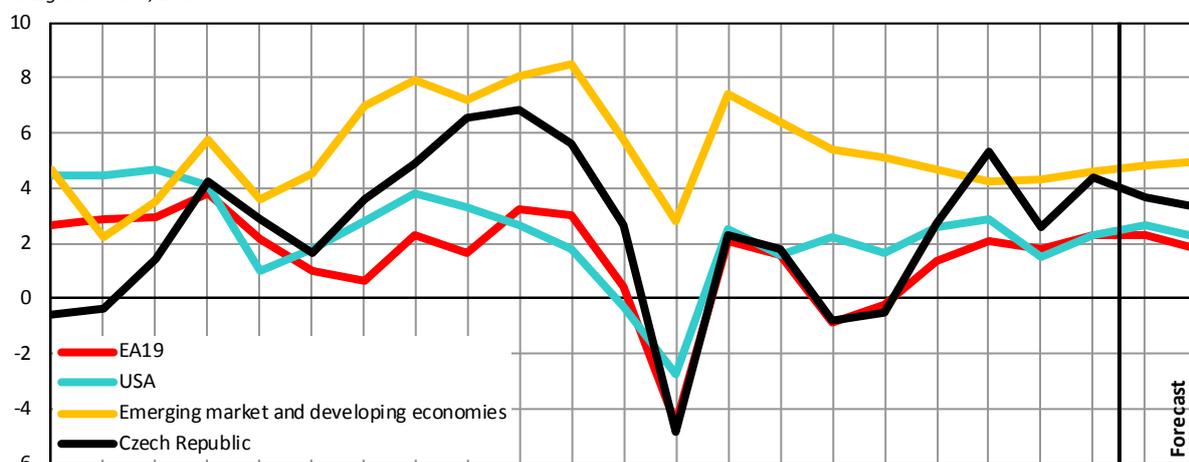
YoY real growth rate, in %

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
									Forecast	Forecast
<b>World</b>	5.4	4.3	3.5	3.5	3.6	3.4	3.2	3.6	3.7	3.7
<b>USA</b>	2.5	1.6	2.2	1.7	2.6	2.9	1.5	2.3	2.7	2.2
<b>China</b>	10.6	9.5	7.9	7.8	7.3	6.9	6.7	6.9	6.8	6.7
<b>EU28</b>	2.1	1.7	-0.4	0.3	1.8	2.3	2.0	2.4	2.4	2.0
<b>EA19</b>	2.1	1.6	-0.9	-0.2	1.3	2.1	1.8	2.3	2.3	1.8
<b>Germany</b>	4.1	3.7	0.5	0.5	1.9	1.7	1.9	2.2	2.4	2.1
<b>France</b>	2.0	2.1	0.2	0.6	0.9	1.1	1.2	1.8	2.1	1.7
<b>United Kingdom</b>	1.7	1.5	1.5	2.1	3.1	2.3	1.9	1.7	1.3	1.2
<b>Austria</b>	1.8	2.9	0.7	0.0	0.8	1.1	1.5	2.9	2.8	2.1
<b>Hungary</b>	0.7	1.7	-1.6	2.1	4.2	3.4	2.2	4.0	3.9	3.0
<b>Poland</b>	3.6	5.0	1.6	1.4	3.3	3.8	2.9	4.6	3.9	3.4
<b>Slovakia</b>	5.0	2.8	1.7	1.5	2.8	3.9	3.3	3.4	3.7	3.9
<b>Czech Republic</b>	2.3	1.8	-0.8	-0.5	2.7	5.3	2.6	4.4	3.6	3.3

Source: CZSO, Eurostat, IMF, NBS China. Calculations of the MoF.

**Graph 1.1.5: Gross Domestic Product**

YoY real growth rate, in %



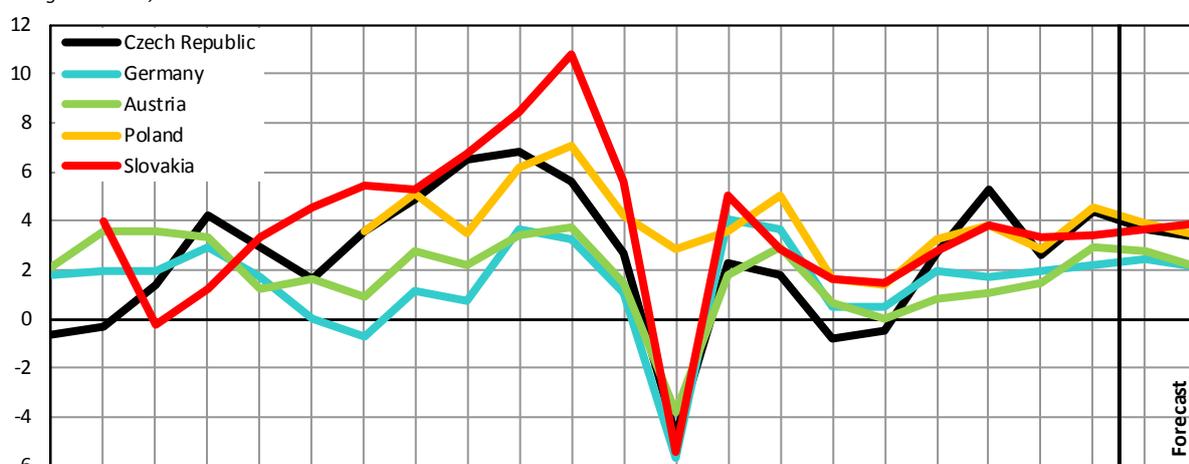
1997 1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019

Note: Emerging market and developing economies comprising 154 countries (according to the IMF's classification)

Source: Eurostat, IMF. Calculations of the MoF.

**Graph 1.1.6: Gross Domestic Product – Czech Republic and the neighbouring states**

YoY real growth rate, in %



1997 1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019

Source: Eurostat. Calculations of the MoF.

**Table 1.1.2: Gross Domestic Product – quarterly**

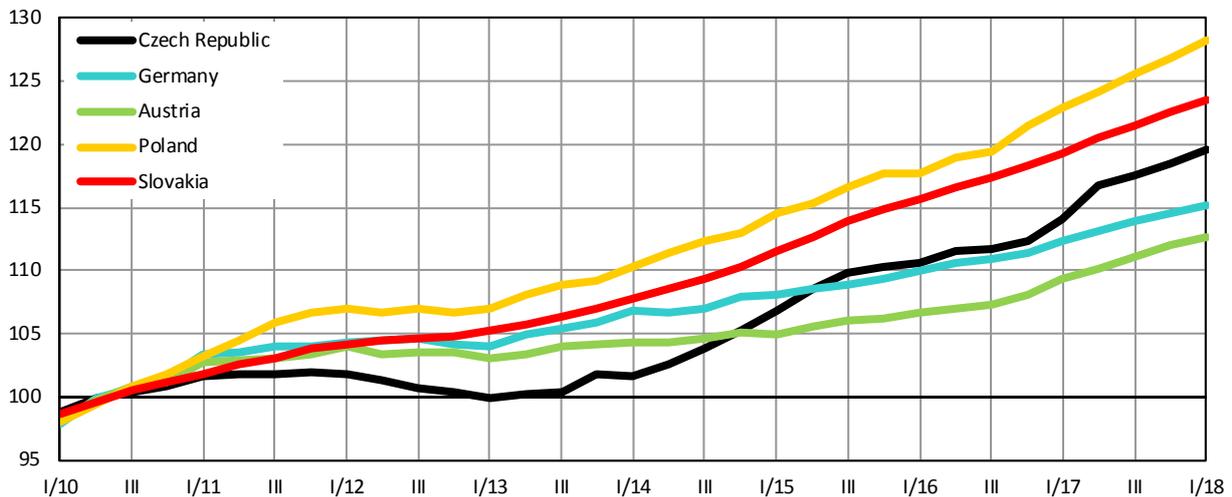
real growth rate, in %, seasonally adjusted data

		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
						<i>Estimate</i>	<i>Forecast</i>	<i>Forecast</i>	<i>Forecast</i>
<b>USA</b>	QoQ	<b>0.3</b>	<b>0.8</b>	<b>0.8</b>	<b>0.7</b>	<b>0.5</b>	<b>0.7</b>	<b>0.7</b>	<b>0.6</b>
	YoY	2.0	2.2	2.3	2.6	2.8	2.7	2.6	2.5
<b>China</b>	QoQ	<b>1.4</b>	<b>1.9</b>	<b>1.8</b>	<b>1.6</b>	<b>1.6</b>	<b>1.8</b>	<b>1.4</b>	<b>1.5</b>
	YoY	6.9	6.9	6.8	6.8	7.1	7.0	6.6	6.4
<b>EU28</b>	QoQ	<b>0.6</b>	<b>0.7</b>	<b>0.7</b>	<b>0.6</b>	<b>0.6</b>	<b>0.5</b>	<b>0.5</b>	<b>0.5</b>
	YoY	2.2	2.5	2.7	2.6	2.6	2.4	2.2	2.1
<b>EA19</b>	QoQ	<b>0.6</b>	<b>0.7</b>	<b>0.7</b>	<b>0.6</b>	<b>0.5</b>	<b>0.5</b>	<b>0.5</b>	<b>0.4</b>
	YoY	2.1	2.4	2.7	2.7	2.5	2.3	2.1	1.9
<b>Germany</b>	QoQ	<b>0.9</b>	<b>0.6</b>	<b>0.7</b>	<b>0.6</b>	<b>0.5</b>	<b>0.6</b>	<b>0.5</b>	<b>0.5</b>
	YoY	2.1	2.3	2.7	2.9	2.5	2.5	2.2	2.1
<b>France</b>	QoQ	<b>0.7</b>	<b>0.6</b>	<b>0.5</b>	<b>0.7</b>	<b>0.5</b>	<b>0.4</b>	<b>0.4</b>	<b>0.4</b>
	YoY	1.2	1.9	2.3	2.5	2.3	2.1	2.0	1.7
<b>United Kingdom</b>	QoQ	<b>0.2</b>	<b>0.3</b>	<b>0.5</b>	<b>0.4</b>	<b>0.3</b>	<b>0.3</b>	<b>0.3</b>	<b>0.2</b>
	YoY	2.0	1.8	1.8	1.4	1.5	1.5	1.3	1.1
<b>Austria</b>	QoQ	<b>1.2</b>	<b>0.7</b>	<b>0.8</b>	<b>0.8</b>	<b>0.6</b>	<b>0.5</b>	<b>0.4</b>	<b>0.5</b>
	YoY	2.6	2.9	3.5	3.6	3.0	2.8	2.3	2.0
<b>Hungary</b>	QoQ	<b>1.5</b>	<b>1.0</b>	<b>1.0</b>	<b>1.3</b>	<b>1.0</b>	<b>0.7</b>	<b>0.8</b>	<b>0.7</b>
	YoY	4.0	3.8	4.3	4.9	4.4	4.0	3.8	3.2
<b>Poland</b>	QoQ	<b>1.1</b>	<b>1.0</b>	<b>1.2</b>	<b>1.0</b>	<b>1.1</b>	<b>0.9</b>	<b>0.8</b>	<b>0.8</b>
	YoY	4.4	4.3	5.2	4.3	4.3	4.3	3.8	3.6
<b>Slovakia</b>	QoQ	<b>0.8</b>	<b>1.0</b>	<b>0.8</b>	<b>0.9</b>	<b>0.8</b>	<b>1.0</b>	<b>1.1</b>	<b>0.9</b>
	YoY	3.1	3.4	3.5	3.5	3.5	3.5	3.8	3.9
<b>Czech Republic</b>	QoQ	<b>1.5</b>	<b>2.4</b>	<b>0.7</b>	<b>0.8</b>	<b>1.0</b>	<b>0.8</b>	<b>0.6</b>	<b>0.6</b>
	YoY	3.0	4.6	5.2	5.5	5.0	3.3	3.2	3.0

Source: Eurostat, NBS China. Calculations of the MoF.

**Graph 1.1.7: Gross Domestic Product – Czech Republic and the neighbouring states**

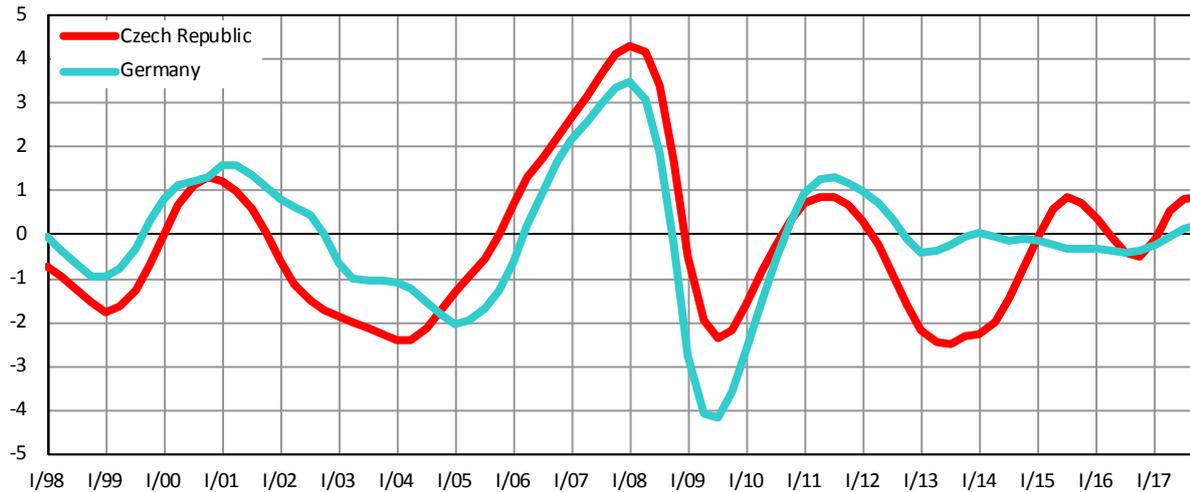
2010=100, seasonally adjusted data, constant prices



Source: Eurostat. Calculations of the MoF.

**Graph 1.1.8: Cyclical Component of GDP – Czech Republic and Germany**

*in % of GDP, derived using the Hodrick-Prescott filter*



Source: Eurostat. Calculations of the MoF.

**Table 1.1.3: Prices of Selected Commodities – yearly**

*spot prices*

		2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	
											Forecast	Forecast
<b>Crude oil Brent</b>	<i>USD/barrel</i>	<b>79.6</b>	<b>111.3</b>	<b>111.5</b>	<b>108.6</b>	<b>99.0</b>	<b>52.4</b>	<b>43.6</b>	<b>54.2</b>	<b>65</b>	<b>61</b>	
	<i>growth in %</i>	29.3	39.8	0.2	-2.6	-8.8	-47.1	-16.9	24.3	20.4	-5.9	
<b>Crude oil Brent index (in CZK)</b>	<i>2010=100</i>	<b>100.0</b>	<b>129.5</b>	<b>143.8</b>	<b>139.9</b>	<b>134.6</b>	<b>85.0</b>	<b>70.1</b>	<b>83.1</b>	<b>88</b>	<b>81</b>	
	<i>growth in %</i>	31.3	29.5	11.0	-2.7	-3.8	-36.9	-17.4	18.5	5.7	-7.8	
<b>Natural gas</b>	<i>USD/MMBtu</i>	<b>8.3</b>	<b>10.5</b>	<b>11.5</b>	<b>11.8</b>	<b>10.1</b>	<b>7.3</b>	<b>4.6</b>	<b>5.6</b>	.	.	
	<i>growth in %</i>	-4.9	26.9	9.1	2.7	-14.7	-27.8	-37.2	23.9	.	.	
<b>Natural gas index (in CZK)</b>	<i>2010=100</i>	<b>100.0</b>	<b>117.9</b>	<b>142.2</b>	<b>145.9</b>	<b>131.7</b>	<b>113.0</b>	<b>70.6</b>	<b>83.4</b>	.	.	
	<i>growth in %</i>	-6.2	17.9	20.6	2.6	-9.8	-14.2	-37.6	18.1	.	.	

Source: CNB, IMF, U. S. Energy Information Administration. Calculations of the MoF.

**Table 1.1.4: Prices of Selected Commodities – quarterly**

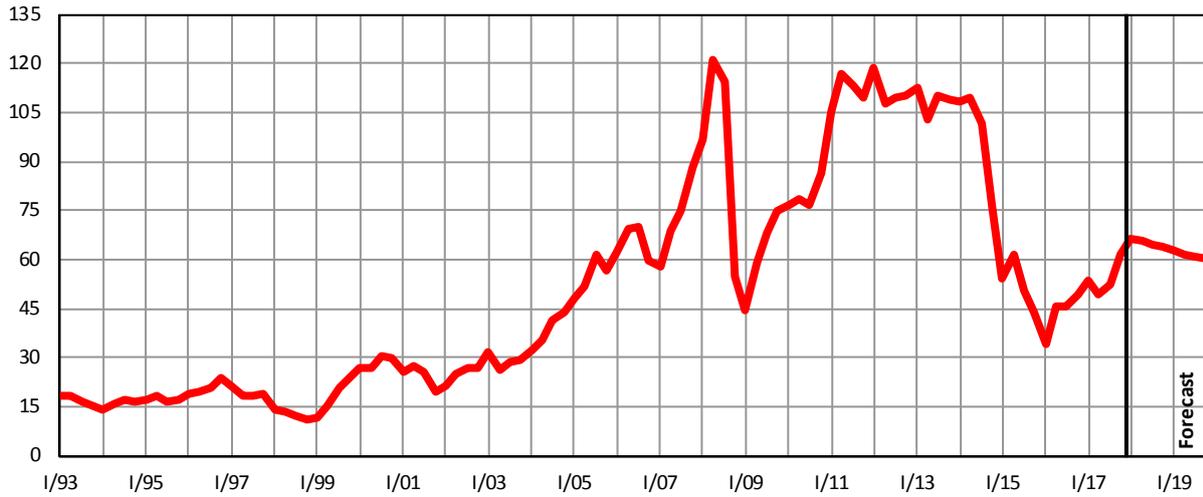
*spot prices*

		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
						Estimate	Forecast	Forecast	Forecast
<b>Crude oil Brent</b>	<i>USD/barrel</i>	<b>53.6</b>	<b>49.6</b>	<b>52.1</b>	<b>61.4</b>	<b>67</b>	<b>66</b>	<b>65</b>	<b>64</b>
	<i>growth in %</i>	58.6	8.8	13.8	25.1	24.3	32.8	24.3	3.7
<b>Crude oil Brent index (in CZK)</b>	<i>2010=100</i>	<b>89.6</b>	<b>78.7</b>	<b>76.1</b>	<b>88.1</b>	<b>91</b>	<b>89</b>	<b>87</b>	<b>85</b>
	<i>growth in %</i>	64.0	9.4	4.3	8.7	1.2	13.1	14.1	-3.7
<b>Natural gas</b>	<i>USD/MMBtu</i>	<b>5.7</b>	<b>5.3</b>	<b>5.3</b>	<b>6.2</b>	.	.	.	.
	<i>growth in %</i>	17.8	30.1	21.3	26.9	.	.	.	.
<b>Natural gas index (in CZK)</b>	<i>2010=100</i>	<b>91.5</b>	<b>81.3</b>	<b>74.9</b>	<b>85.8</b>	.	.	.	.
	<i>growth in %</i>	21.8	30.9	11.2	10.4	.	.	.	.

Source: CNB, U. S. Energy Information Administration, World Bank. Calculations of the MoF.

### Graph 1.1.9: Dollar Prices of Oil

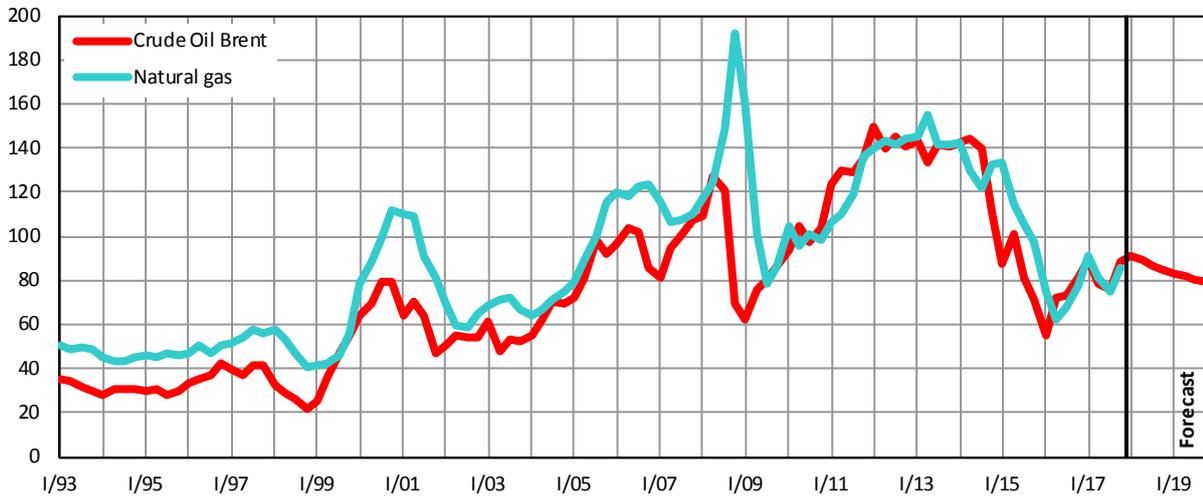
USD/barrel



Source: U. S. Energy Information Administration. Calculations of the MoF.

### Graph 1.1.10: Koruna Indices of Prices of Selected Commodities

index 2010=100



Source: CNB, U.S. Energy Information Administration, World Bank. Calculations of the MoF.

## 1.2 Fiscal Policy

On the basis of the data released by the CZSO the balance of the general government sector ended in a surplus of CZK 80.6 billion (*versus CZK 56.6 billion*) in 2017, which corresponds to 1.6% of GDP (*versus 1.1% of GDP*). Unlike in the previous year, all subsectors contributed positively to the highest surplus of the general government sector in the entire available time series (since 1995). The structural balance improved moderately to 1.1% of GDP, the primary structural balance remained unchanged at 1.8% of GDP.

The improved budget performance of the general government sector was to a large extent determined by public budgets' revenues, within which tax revenues – including social security contributions – were 7.7% higher than in 2016. The most dynamic taxes were those that were affected by not only the economic developments but also by the measures against tax evasion, especially electronic VAT reporting and electronic registration of sales. The impact in 2017 of these measures is estimated at CZK 14 billion in the case of VAT (growth of 9.5%), the contribution of electronic registration of sales to revenues from the personal income tax (growth of 11.4%) and social security contributions (growth of 8.0%) was CZK 8 billion. The corporate income tax revenues (YoY growth of 4.3%) also reflected the positive effect (CZK 1.7 billion) of electronic registration of sales, though to a lesser extent than in the case of the aforementioned taxes.

Revenues from excise duties rose by 3.1% YoY. This development was mainly driven by growing real consumption of households and the increase in the tax rate on tobacco products.

Total expenditures increased by 4.2%. In comparison with 2016 the growth was primarily affected by final consumption expenditures of the general government sector (growth of 5.4%), especially compensation of employees (10.2%). The growth in compensation was driven by salary raises since November 2016 as well as by increases in salary scales in certain segments of the general government sector since July and November 2017. Apart from final consumption expenditures, the expenditures on social benefits (2.8%) and investments in fixed capital (8.6%) also rose. National resources financed two thirds of gross fixed capital formation expenditures, while the EU funds covered the remaining part.

On the other hand, interest expenditures decreased for the third time in a row, by almost 14% in 2017. This corresponded to a saving of CZK 6 billion. The level of interest expenditures thus dropped below that of the year 2007. It was the result of a combination of a couple of factors, including good emission timing and a flexible response of the MoF to the developments in financial markets.

We expect the balance of the general government sector to reach a surplus amounting to 1.5% of GDP (*versus 1.3% of GDP*) in 2018, out of which the surplus of local governments should account for more than 60%. From the perspective of the structural balance there should be a small YoY decrease in the surplus by 0.3 pp to 0.8% of GDP.

In 2018 the revenues of the general government sector should grow at the same pace as in 2017 (by 6.4%), with tax revenues having the dominant effect, just like in the last year. Key measures to fight tax evasion will be a positive factor, though to a lesser extent than in 2017. Above all, the estimate of the impact of electronic registration of sales has been adjusted, reflecting the delayed launch of the third and the fourth phase due to the decision of the Constitutional Court. The electronic registration of sales should have applied to additional entities with the effect from March and June 2018, respectively; now the extension is proposed to be launched in one wave in the course of 2019.

The dynamics of direct taxes should slow down in 2018 due to the corporate income tax; nevertheless, we still expect the revenues from income taxes to increase by 6.8%. This should be primarily driven by more than 12% growth in personal income tax. Similarly to the previous year, there should be a positive effect not just of the forecasted 7.7% growth in the wage bill but also of the change in the distribution of wages and salaries following the increase in the minimum and guaranteed wages. Both these factors, together with more than 5% increase in the assessment base for the payment for state insured persons, should determine also social security contributions.

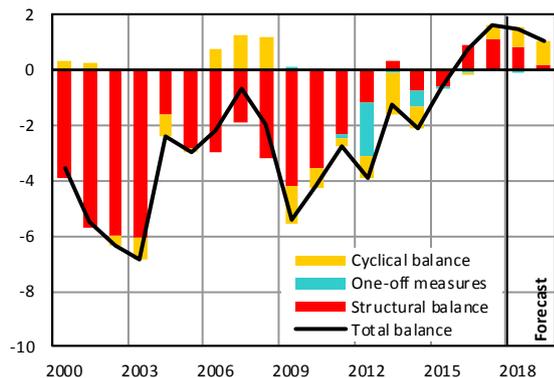
On the expenditure side we expect final consumption expenditures of the general government sector to slow moderately down towards 5% this year. Similarly to the last year, the growth should be driven by strong dynamics of compensation of employees (7.5%); intermediate consumption and social transfers in kind are expected to accelerate moderately in comparison with the previous year.

Within other expenditures, the cash social benefits, which are expected to increase by almost 6% in 2018, reflect the discretionary measures approved last year and economic developments. Investment expenditures are expected to be up by close to 15%, supported by stronger start of projects from the 2014–2020 financial perspective. With respect to the assumed monetary policy developments in the CR we expect a gradual rise in interest rates, which will probably reverse the existing trend of decreasing interest expenditures.

With the envisaged surplus of the whole general government sector the debt to GDP ratio is expected to decline further to 32.9% (*versus 33.1%*) at the end of 2018.

**Graph 1.2.1: Decomposition of the Government Balance**

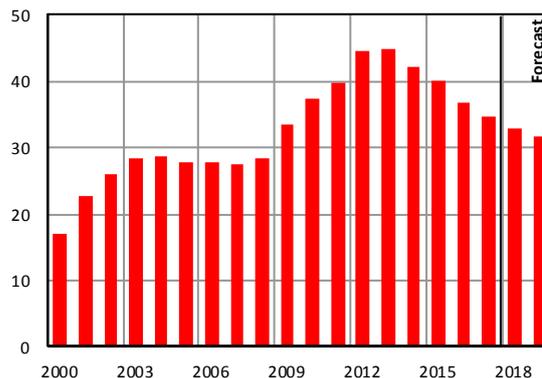
in % of GDP



Source: CZSO. Calculations of the MoF.

**Graph 1.2.2: General Government Debt**

in % of GDP



Source: CZSO. Calculations of the MoF.

**Table 1.2.1: Net Lending/Borrowing and Debt**

		2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	
											Forecast	Forecast
<b>General government balance</b>	% GDP	-4.2	-2.7	-3.9	-1.2	-2.1	-0.6	0.7	1.6	1.5	1.1	
	bill. CZK	-166	-110	-160	-51	-91	-28	35	81	79	59	
<b>Cyclical balance</b>	% GDP	-0.7	-0.3	-0.8	-1.5	-0.8	0.1	-0.1	0.5	0.7	0.9	
<b>Cyclically adjusted balance</b>	% GDP	-3.5	-2.5	-3.1	0.2	-1.3	-0.7	0.8	1.1	0.7	0.2	
<b>One-off measures <sup>1)</sup></b>	% GDP	0.1	-0.2	-1.9	-0.1	-0.6	-0.1	-0.1	0.0	-0.1	0.0	
<b>Structural balance</b>	% GDP	-3.6	-2.3	-1.1	0.4	-0.8	-0.6	0.9	1.1	0.8	0.2	
<b>Fiscal effort <sup>2)</sup></b>	pp	0.7	1.2	1.2	1.5	-1.1	0.1	1.5	0.2	-0.3	-0.7	
<b>Interest expenditure</b>	% GDP	1.3	1.3	1.4	1.3	1.3	1.1	0.9	0.7	0.7	0.8	
<b>Primary balance</b>	% GDP	-2.9	-1.4	-2.5	0.1	-0.8	0.5	1.6	2.3	2.2	1.8	
<b>Cyclically adjusted primary balance</b>	% GDP	-2.2	-1.2	-1.7	1.6	0.0	0.4	1.7	1.8	1.5	0.9	
<b>General government debt</b>	% GDP	37.4	39.8	44.5	44.9	42.2	40.0	36.8	34.6	32.9	31.6	
	bill. CZK	1 480	1 606	1 805	1 840	1 819	1 836	1 755	1 749	1 748	1 769	
<b>Change in debt-to-GDP ratio</b>	pp	3.8	2.5	4.6	0.4	-2.7	-2.2	-3.2	-2.2	-1.7	-1.2	

<sup>1)</sup> One-off and temporary measures are such measures that have only a temporary impact on public budgets. Besides their temporary impact on overall balance, these measures are usually of non-recurring nature and very often result from the events that are beyond the direct power of the government.

<sup>2)</sup> Change in structural balance.

Source: CZSO. Calculations of the MoF.

## 1.3 Monetary Policy, Financial Sector and Exchange Rates

### 1.3.1 Monetary Policy

Following the discontinuation of its exchange rate commitment in April 2017, the CNB implements monetary policy in a standard regime, in which interest rates are the main tool. At the beginning of February, it raised the two-week repo rate by 0.25 pp to 0.75%. Monetary conditions are thus gradually tightening in the exchange rate as well as the interest rate components. We expect this development to continue also in the forecast horizon. In 2018, monetary conditions should be tightening mainly in the exchange rate component.

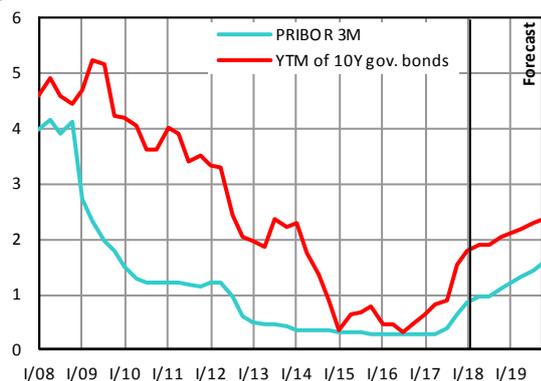
### 1.3.2 Financial Sector and Interest Rates

In the first quarter of 2018, the **3M** (three-month) **PRIBOR** rate increased to 0.9% (*in line with the forecast*). Due to the adjustment to assumptions about monetary policy developments (also in connection with a revision of the exchange rate forecast in the direction of stronger koruna), we expect that the 3M PRIBOR rate will average 1.0% (*versus 1.1%*) in 2018 and further increase to the average 1.4% (*versus 1.7%*) in 2019.

Long-term interest rates have recently been increasing gradually as a result of the expected tightening of monetary policy. The **yield to maturity on 10-year government bonds** for convergence purposes was 1.8% in January and February 2018. If the long-term rates remained at that level also in March, the average for the first quarter would be 0.2 pp higher than in the last forecast. With regard to the expected inflation rate and the CNB's and ECB's monetary policy stance, we expect that long-term interest rates will continue to grow. On average, they could thus reach 1.9% (*versus 1.7%*) in 2018 and 2.2% (*versus 2.0%*) in 2019.

**Graph 1.3.1: Interest Rates**

in% p.a.



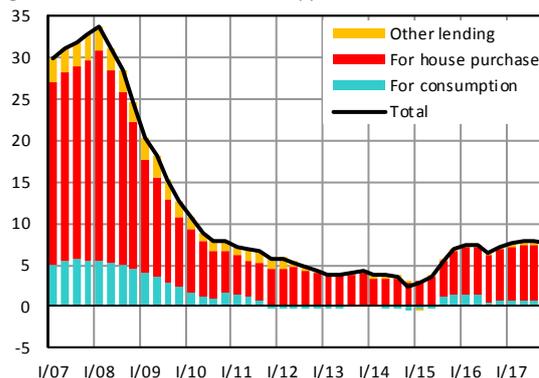
Source: CNB. Calculations of the MoF.

In the fourth quarter of 2017, loans to households increased by 7.6%, and their dynamics thus slightly decreased in comparison with the previous quarter. Growth slowed down for all groups of loans, i.e. housing loans, loans for consumption and other loans (loans to tradesmen).

Due to the structure of loans to households, their growth has long been driven by housing loans (their weight is approximately 75%). Housing loans acceleration that has taken place since the beginning of 2015 and has been supported by low interest rates, combined with a limited supply of residential real estate, led to a dynamic growth in real estate prices. Continuation of this trend would pose a negative risk for the economy (mainly households).

**Graph 1.3.2: Loans to Households**

YoY growth rate in%, contributions in pp



Source: CNB. Calculations of the MoF.

The growth in housing loans slowed down slightly since mid-2017 – it hovered just under 9% in the fourth quarter of 2017 and January 2018. A certain cooling of the housing loans market is also testified by data on genuinely new housing loans<sup>1</sup> that banks lent to households. Whereas between the first quarter of 2015 and the second quarter of 2017, the YoY growth in these loans exceeded 20% on average, there was a decline by almost 3% in the second half of 2017. That was probably due to higher interest rates, CNB's recommendations on the loan-to-value ratio and the reached high level of real estate prices, which has significantly reduced the availability of own housing even for medium-income groups. However, the data on residential construction and issued building permits suggest that the supply of flats should increase in the future, which would act against the growth in their prices.

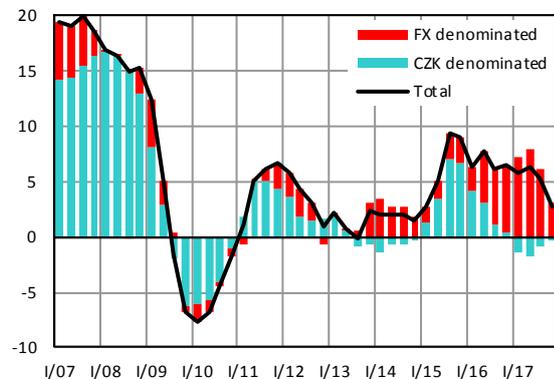
In comparison with the previous quarter, the YoY growth in total loans to non-financial corporations decreased to 2.6% in the fourth quarter of 2017, mainly due to a decrease in the dynamics of medium- and long-term loans. Good financial situation of companies could have also played a role as they could have largely financed their expenditures from their own resources. A slight decrease in the koruna loans (-0.5%) and an increase in foreign currency loans continued; however, the latter significantly slowed down (to 11.5%). These trends may reflect in-

<sup>1</sup> Include loans that entered the economy for the first time in the respective period. Increases in refinanced and existing loans are also reported in net new loans.

creased uncertainty about the further development of the koruna exchange rate, possibly also speculations on the koruna appreciation. However, they may also be the result of behaviour of exporters seeking natural hedging.

### Graph 1.3.3: Loans to Non-financial Corporations

YoY growth rate in%, contributions in pp

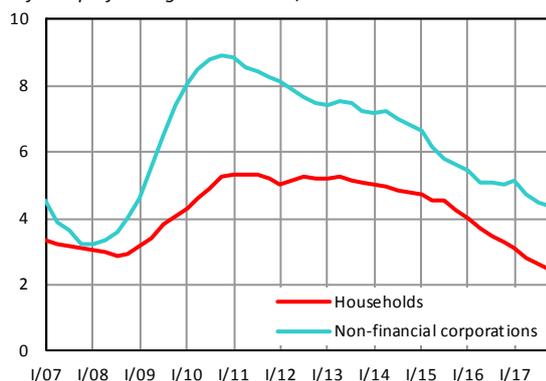


Source: CNB. Calculations of the MoF.

The share of non-performing loans in total loans reflects the positive economic development. In the fourth quarter of 2017, it was 2.4% for household and 4.3% for non-financial corporations. The low and long declining share of non-performing loans shows a very good financial condition of households and companies. However, in the case of loans to households, approximately one fifth of consumer loans is provided by non-bank intermediaries. According to the 2016/2017 Financial Stability Report, the default rate of these loans is approximately three times higher than that of consumer loans provided by banks. The situation for loans to non-financial corporations is the opposite – loans from non-bank intermediaries (mainly leasing) show a slightly lower default rate than bank loans.

### Graph 1.3.4: Non-performing Loans

ratio of non-performing to total loans, in%



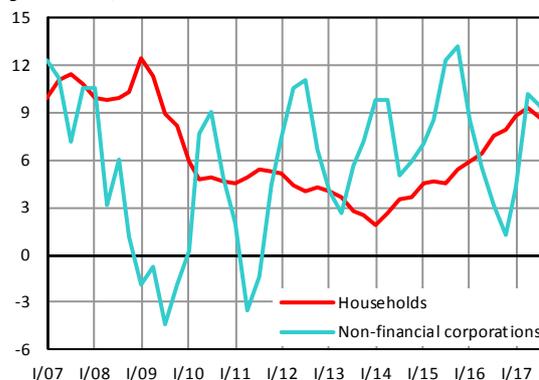
Source: CNB. Calculations of the MoF.

The YoY deposit growth decreased to 8.0% for households and 7.7% for non-financial corporations in the

fourth quarter of 2017. In terms of financing future consumption and investment from own resources, the continued growth of deposits may be assessed positively.

### Graph 1.3.5: Deposits

YoY growth rate, in%



Source: CNB. Calculations of the MoF.

### 1.3.3 Exchange Rates

The koruna continued to strengthen against the euro at the beginning of 2018, but at the beginning of February it started weakening gradually from levels around 25.20 CZK/EUR, and the exchange rate mostly oscillated above 25.40 CZK/EUR in March. The developments of the exchange rate were probably influenced by a change in expectations about interest rate hikes by the CNB, and thus also about the level of the interest rate differential vis-à-vis the Euro Area. The exchange rate averaged 25.40 CZK/EUR in the first quarter of 2018 (versus 25.5 CZK/EUR) and appreciated by 6.4% YoY.

We expect that the koruna will gradually appreciate against the euro in the forecast and outlook horizon. In addition to the continuing economic convergence, the appreciation trend will also be supported by a positive interest differential vis-à-vis the Euro Area. On average, the exchange rate could be 25.1 CZK/EUR (versus 25.4 CZK/EUR) in 2018 and 24.7 CZK/EUR (versus 25.0 CZK/EUR) in 2019. A factor of uncertainty regarding further developments of the exchange rate is not only the future monetary policy stance (or a change in market expectations about adjustments to monetary policy interest rates) but also speculative koruna positions of foreign investors.

The expected development of the CZK/USD exchange rate is implied by the USD/EUR exchange rate, for which a technical assumption of stability at the level of 1.23 USD/EUR (the average of the last 10 trading days before the cut-off date for the input data for the forecast) has been adopted.

**Table 1.3.1: Interest Rates – yearly**  
average of period, unless stated otherwise

		2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
										Forecast	Forecast
<b>Repo 2W rate CNB</b> (end of period)	in % p.a.	0.75	0.75	0.05	0.05	0.05	0.05	0.05	0.50	.	.
<b>Main refinancing rate ECB</b> (end of period)	in % p.a.	1.00	1.00	0.75	0.25	0.05	0.05	0.05	0.00	.	.
<b>Federal funds rate</b> (end of period)	in % p.a.	0.25	0.25	0.25	0.25	0.25	0.50	0.75	1.50	.	.
<b>PRIBOR 3M</b>	in % p.a.	1.31	1.19	1.00	0.46	0.36	0.31	0.29	0.41	1.0	1.4
<b>YTM of 10Y government bonds</b>	in % p.a.	3.88	3.71	2.78	2.11	1.58	0.61	0.43	0.98	1.9	2.2
<b>Client interest rates</b>											
<b>Loans to households</b>	in % p.a.	7.01	6.84	6.47	6.05	5.59	5.15	4.65	4.10	.	.
<b>Loans to non-financial corporations</b>	in % p.a.	4.11	3.94	3.72	3.20	3.01	2.78	2.59	2.57	.	.
<b>Deposits of households</b>	in % p.a.	1.25	1.20	1.18	1.02	0.85	0.65	0.47	0.36	.	.
<b>Deposits of non-financial corporations</b>	in % p.a.	0.56	0.51	0.56	0.41	0.29	0.19	0.10	0.05	.	.

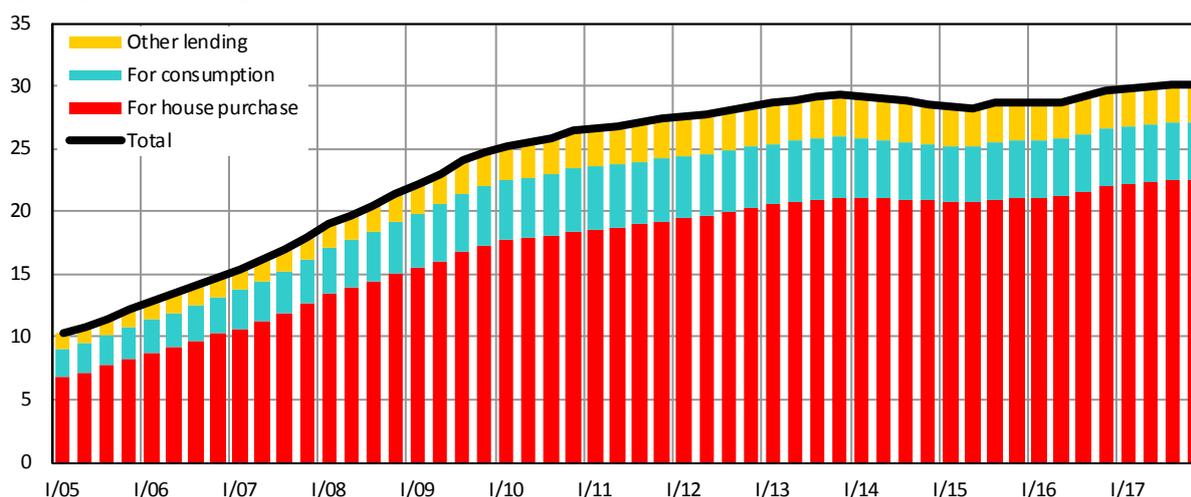
Source: CNB, ECB, Fed. Calculations of the MoF.

**Table 1.3.2: Interest Rates – quarterly**  
average of period, unless stated otherwise

		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
						Estimate	Forecast	Forecast	Forecast
<b>Repo 2W rate CNB</b> (end of period)	in % p.a.	0.05	0.05	0.25	0.50	0.75	.	.	.
<b>Main refinancing rate ECB</b> (end of period)	in % p.a.	0.00	0.00	0.00	0.00	0.00	.	.	.
<b>Federal funds rate</b> (end of period)	in % p.a.	1.00	1.25	1.25	1.50	1.75	.	.	.
<b>PRIBOR 3M</b>	in % p.a.	0.28	0.29	0.40	0.65	0.86	1.0	1.0	1.1
<b>YTM of 10Y government bonds</b>	in % p.a.	0.66	0.82	0.90	1.54	1.8	1.9	1.9	2.0
<b>Client interest rates</b>									
<b>Loans to households</b>	in % p.a.	4.29	4.15	4.04	3.94	.	.	.	.
<b>Loans to non-financial corporations</b>	in % p.a.	2.57	2.55	2.53	2.64	.	.	.	.
<b>Deposits of households</b>	in % p.a.	0.38	0.36	0.35	0.34	.	.	.	.
<b>Deposits of non-financial corporations</b>	in % p.a.	0.06	0.05	0.05	0.04	.	.	.	.

Source: CNB, ECB, Fed. Calculations of the MoF.

**Graph 1.3.6: Loans to Households**  
in % of GDP (from yearly moving sums)



Source: CNB, CZSO. Calculations of the MoF.

**Table 1.3.3: Loans and Deposits – yearly averages**

		2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
<b>Households</b>											
<b>Loans</b>	<i>growth in %</i>	<b>29.2</b>	<b>16.5</b>	<b>8.9</b>	<b>6.6</b>	<b>5.0</b>	<b>4.0</b>	<b>3.4</b>	<b>4.8</b>	<b>7.2</b>	<b>7.8</b>
For consumption	<i>growth in %</i>	25.7	16.4	7.3	4.2	-1.0	-0.1	-0.9	3.4	6.0	4.3
For house purchase	<i>growth in %</i>	30.8	15.5	8.9	6.5	6.4	5.5	4.5	5.6	8.1	9.0
Other lending	<i>growth in %</i>	24.9	23.9	11.6	11.1	6.0	1.2	2.9	1.0	3.0	4.2
CZK denominated	<i>growth in %</i>	29.3	16.5	8.8	6.6	4.9	4.0	3.4	4.7	7.2	7.7
FX denominated	<i>growth in %</i>	-8.9	0.1	31.0	2.4	30.8	-1.3	0.0	12.7	8.5	36.3
<b>Deposits</b>	<i>growth in %</i>	<b>10.0</b>	<b>10.2</b>	<b>5.1</b>	<b>5.0</b>	<b>4.5</b>	<b>3.3</b>	<b>2.9</b>	<b>4.8</b>	<b>7.0</b>	<b>8.7</b>
CZK denominated	<i>growth in %</i>	10.7	10.1	5.6	5.4	4.7	3.3	2.7	4.1	6.9	9.7
FX denominated	<i>growth in %</i>	-3.4	13.1	-6.8	-4.0	-2.1	2.3	8.5	22.5	7.3	-13.9
<b>Non-performing loans (banking statistics)</b>	<i>share, in %</i>	<b>3.0</b>	<b>3.6</b>	<b>4.8</b>	<b>5.3</b>	<b>5.2</b>	<b>5.2</b>	<b>4.9</b>	<b>4.5</b>	<b>3.6</b>	<b>2.7</b>
<b>Loans to deposits ratio</b>	<i>in %</i>	<b>56</b>	<b>59</b>	<b>61</b>	<b>62</b>	<b>63</b>	<b>63</b>	<b>63</b>	<b>63</b>	<b>63</b>	<b>63</b>
<b>Non-financial corporations</b>											
<b>Loans</b>	<i>growth in %</i>	<b>15.9</b>	<b>1.9</b>	<b>-5.2</b>	<b>4.7</b>	<b>3.5</b>	<b>1.3</b>	<b>1.9</b>	<b>6.5</b>	<b>6.6</b>	<b>5.0</b>
CZK denominated	<i>growth in %</i>	18.7	0.5	-5.2	4.9	2.6	0.3	-1.0	5.9	2.8	-1.4
FX denominated	<i>growth in %</i>	3.4	9.1	-5.4	3.7	7.8	5.7	13.7	9.0	20.5	24.4
<b>Deposits</b>	<i>growth in %</i>	<b>5.1</b>	<b>-2.2</b>	<b>5.5</b>	<b>0.4</b>	<b>8.9</b>	<b>4.9</b>	<b>7.6</b>	<b>10.3</b>	<b>4.6</b>	<b>7.9</b>
CZK denominated	<i>growth in %</i>	6.4	-3.2	6.9	2.0	8.2	4.2	5.6	6.7	4.5	14.0
FX denominated	<i>growth in %</i>	0.5	1.6	0.2	-6.1	11.8	8.0	15.2	23.2	4.8	-11.1
<b>Non-performing loans (banking statistics)</b>	<i>share, in %</i>	<b>3.5</b>	<b>6.0</b>	<b>8.6</b>	<b>8.5</b>	<b>7.8</b>	<b>7.4</b>	<b>7.0</b>	<b>6.0</b>	<b>5.2</b>	<b>4.7</b>
<b>Loans to deposits ratio</b>	<i>in %</i>	<b>129</b>	<b>135</b>	<b>121</b>	<b>126</b>	<b>120</b>	<b>116</b>	<b>110</b>	<b>106</b>	<b>108</b>	<b>105</b>

Note: All indicators, except for the share of non-performing loans, are from the monetary statistics.

Source: CNB, ECB. Calculations of the MoF.

**Table 1.3.4: Loans and Deposits – quarterly averages**

		2016				2017			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<b>Households</b>									
<b>Loans</b>	<i>growth in %</i>	<b>7.5</b>	<b>7.5</b>	<b>6.6</b>	<b>7.2</b>	<b>7.6</b>	<b>8.0</b>	<b>8.0</b>	<b>7.6</b>
For consumption	<i>growth in %</i>	9.7	8.7	2.3	3.7	4.2	4.6	4.5	3.9
For house purchase	<i>growth in %</i>	7.7	8.0	8.0	8.5	8.9	9.2	9.2	8.8
Other lending	<i>growth in %</i>	2.7	2.6	3.0	3.5	3.7	4.7	4.4	4.1
CZK denominated	<i>growth in %</i>	7.5	7.5	6.6	7.2	7.6	7.9	7.9	7.5
FX denominated	<i>growth in %</i>	13.1	18.3	6.1	-2.0	12.0	48.5	49.4	35.8
<b>Deposits</b>	<i>growth in %</i>	<b>5.9</b>	<b>6.4</b>	<b>7.6</b>	<b>8.0</b>	<b>8.8</b>	<b>9.3</b>	<b>8.6</b>	<b>8.0</b>
CZK denominated	<i>growth in %</i>	5.7	6.3	7.6	8.2	9.4	10.6	9.8	8.9
FX denominated	<i>growth in %</i>	11.5	8.6	6.6	3.1	-5.6	-18.7	-17.3	-13.7
<b>Non-performing loans (banking statistics)</b>	<i>share, in %</i>	<b>4.0</b>	<b>3.7</b>	<b>3.5</b>	<b>3.3</b>	<b>3.1</b>	<b>2.8</b>	<b>2.6</b>	<b>2.4</b>
<b>Loans to deposits ratio</b>	<i>in %</i>	<b>63</b>	<b>63</b>	<b>63</b>	<b>64</b>	<b>62</b>	<b>62</b>	<b>63</b>	<b>64</b>
<b>Non-financial corporations</b>									
<b>Loans</b>	<i>growth in %</i>	<b>6.3</b>	<b>7.8</b>	<b>6.1</b>	<b>6.4</b>	<b>5.8</b>	<b>6.3</b>	<b>5.3</b>	<b>2.6</b>
CZK denominated	<i>growth in %</i>	5.4	3.8	1.5	0.5	-1.7	-2.3	-1.2	-0.5
FX denominated	<i>growth in %</i>	9.7	22.0	22.7	27.1	31.1	32.6	24.8	11.5
<b>Deposits</b>	<i>growth in %</i>	<b>8.6</b>	<b>5.6</b>	<b>3.2</b>	<b>1.3</b>	<b>4.3</b>	<b>10.2</b>	<b>9.5</b>	<b>7.7</b>
CZK denominated	<i>growth in %</i>	8.0	4.5	3.2	2.4	8.5	19.8	15.6	12.4
FX denominated	<i>growth in %</i>	10.3	8.9	3.0	-2.2	-8.8	-18.0	-9.4	-7.8
<b>Non-performing loans (banking statistics)</b>	<i>share, in %</i>	<b>5.4</b>	<b>5.1</b>	<b>5.1</b>	<b>5.0</b>	<b>5.1</b>	<b>4.7</b>	<b>4.5</b>	<b>4.3</b>
<b>Loans to deposits ratio</b>	<i>in %</i>	<b>104</b>	<b>108</b>	<b>110</b>	<b>109</b>	<b>105</b>	<b>104</b>	<b>106</b>	<b>104</b>

Note: All indicators, except for the share of non-performing loans, are from the monetary statistics.

Source: CNB, ECB. Calculations of the MoF.

**Table 1.3.5: Exchange Rates – yearly**

		2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
								Forecast	Forecast	Outlook	Outlook
<b>Nominal exchange rates</b>											
<b>CZK / EUR</b>	average	<b>25.14</b>	<b>25.97</b>	<b>27.53</b>	<b>27.28</b>	<b>27.03</b>	<b>26.33</b>	<b>25.1</b>	<b>24.7</b>	<b>24.3</b>	<b>23.9</b>
	appreciation in %	-2.2	-3.2	-5.7	0.9	0.9	2.7	4.7	2.0	1.5	1.5
<b>CZK / USD</b>	average	<b>19.58</b>	<b>19.56</b>	<b>20.75</b>	<b>24.60</b>	<b>24.43</b>	<b>23.39</b>	<b>20.4</b>	<b>20.0</b>	<b>19.8</b>	<b>19.5</b>
	appreciation in %	-9.7	0.1	-5.7	-15.7	0.7	4.5	14.4	2.0	1.5	1.5
<b>NEER</b>	average of 2015=100	<b>108.9</b>	<b>106.4</b>	<b>100.8</b>	<b>100.0</b>	<b>102.4</b>	<b>105.4</b>	<b>112</b>	<b>114</b>	<b>115</b>	<b>117</b>
	appreciation in %	-3.5	-2.3	-5.2	-0.8	2.4	2.9	5.9	2.0	1.5	1.5
<b>Real exchange rate to EA19<sup>1)</sup></b>	average of 2010=100	<b>99.8</b>	<b>96.8</b>	<b>92.7</b>	<b>93.3</b>	<b>94.6</b>	<b>97.4</b>	<b>102</b>	<b>105</b>	<b>107</b>	<b>109</b>
	appreciation in %	-2.0	-3.0	-4.2	0.7	1.4	3.0	5.0	2.5	1.9	2.1
<b>REER</b>	average of 2010=100	<b>99.2</b>	<b>96.9</b>	<b>91.8</b>	<b>91.2</b>	<b>93.5</b>	<b>96.8</b>	.	.	.	.
(Eurostat, CPI deflated, 42 countries)	appreciation in %	-2.8	-2.3	-5.2	-0.7	2.5	3.6	.	.	.	.

<sup>1)</sup> Deflated by GDP deflators.

Source: CNB, Eurostat. Calculations of the MoF.

**Table 1.3.6: Exchange Rates – quarterly**

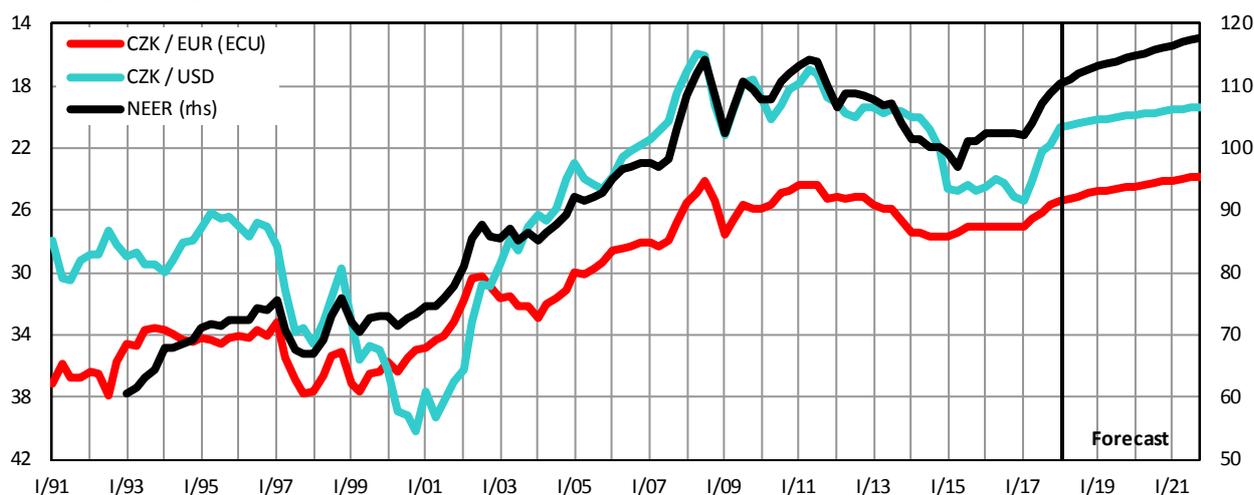
		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
						Estimate	Forecast	Forecast	Forecast
<b>Nominal exchange rates</b>									
<b>CZK / EUR</b>	average	<b>27.02</b>	<b>26.53</b>	<b>26.08</b>	<b>25.65</b>	<b>25.40</b>	<b>25.2</b>	<b>25.1</b>	<b>24.9</b>
	appreciation in %	0.1	1.9	3.6	5.4	6.4	5.2	4.1	3.0
<b>CZK / USD</b>	average	<b>25.38</b>	<b>24.09</b>	<b>22.19</b>	<b>21.79</b>	<b>20.66</b>	<b>20.5</b>	<b>20.4</b>	<b>20.2</b>
	appreciation in %	-3.3	-0.6	9.1	15.0	22.8	17.4	8.9	7.7
<b>NEER</b>	average of 2015=100	<b>101.9</b>	<b>104.0</b>	<b>107.1</b>	<b>108.9</b>	<b>110</b>	<b>111</b>	<b>112</b>	<b>113</b>
	appreciation in %	-0.5	1.6	4.5	6.3	8.3	6.9	4.5	3.5
<b>Real exchange rate to EA19<sup>1)</sup></b>	average of 2010=100	<b>94.6</b>	<b>96.3</b>	<b>98.8</b>	<b>100.3</b>	<b>101</b>	<b>101</b>	<b>103</b>	<b>104</b>
	appreciation in %	-0.1	1.8	4.0	6.5	6.5	5.3	4.4	3.4
<b>REER</b>	average of 2010=100	<b>93.5</b>	<b>95.2</b>	<b>98.5</b>	<b>100.2</b>	.	.	.	.
(Eurostat, CPI deflated, 42 countries)	appreciation in %	-0.6	1.9	5.4	7.7	.	.	.	.

<sup>1)</sup> Deflated by GDP deflators.

Source: CNB, Eurostat. Calculations of the MoF.

**Graph 1.3.7: Nominal Exchange Rates**

quarterly averages, average 2015=100 (rhs)



Source: CNB. Calculations of the MoF.

### Graph 1.3.8: Real Exchange Rate to EA19

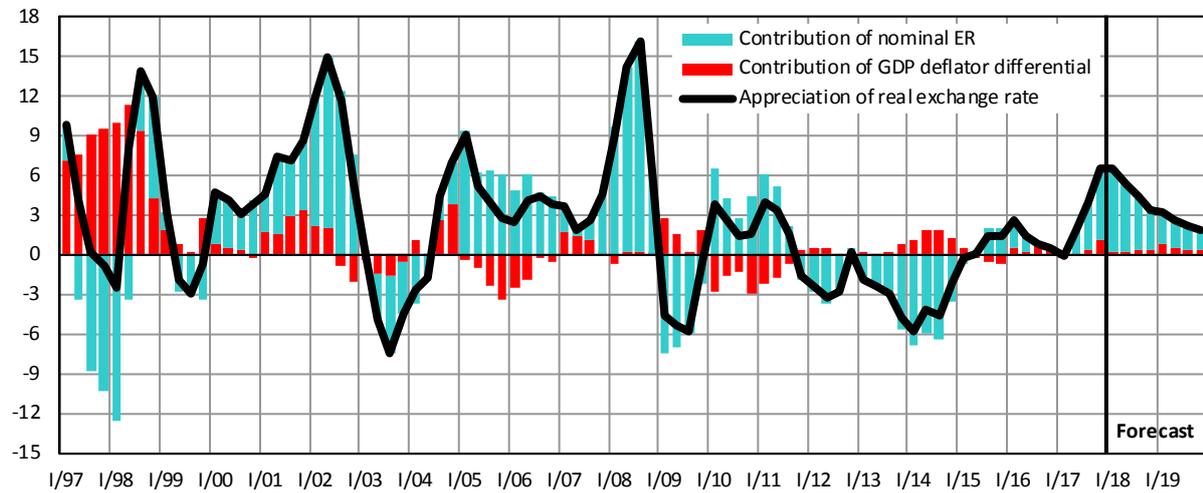
quarterly averages, deflated by GDP deflators, average 2010=100



Source: CNB, Eurostat. Calculations of the MoF.

### Graph 1.3.9: Real Exchange Rate to EA19

deflated by GDP deflators, YoY growth rate in %, contributions in percentage points



Source: CNB, Eurostat. Calculations of the MoF.

## 1.4 Structural Policies

### 1.4.1 Business Environment

On 17 January 2018, the government returned to the legislative process a draft **amendment to the Insolvency Act**, which makes available the institution of debt relief to a wider group of debtors by softening the conditions of debt relief. Debtors will be able to enter the debt relief process regardless of the amount of their debts, and at the same time the condition under which the debtor must be able to pay at least 30% of their debts in five years will be cancelled. The debt relief process will take three, five or seven years. The amendment should become effective on the first day of the fourth calendar month after its promulgation.

### 1.4.2 Social and Health Care Systems

On 1 February 2018, an **amendment to the Health Insurance Act** became effective, which introduced a benefit of one-week paternal postnatal child care.

On 1 February 2018, an **amendment to the Act on Social Security Contributions** became effective, which simplified the system of payment of social security contribu-

tions by self-employed persons. The amendment also increased sickness benefits for long-term patients by 6 pp to 66% of the reduced daily assessment base from the 31st day of the sickness leave and by 12 pp to 72% of the reduced daily assessment base from the 61st day of the sickness leave. The amendment also introduced electronic sick leave certificates with the effect from 1 January 2019.

A draft **amendment to the Act on Pension Insurance**, approved by the government on 27 February 2018, increases the basic pension assessment for newly granted as well as already paid pensions from 9 to 10% of the average wage. It also increases pensions for pensioners who have reached 85 years of age by CZK 1,000 monthly. The amendment should take effect on 1 September 2018 and the new rules on 1 January 2019.

On 27 March 2018 the government approved the introduction of a 75% **discount on bus and train fares** for pupils, students and pensioners aged 65 or above. The discount will be effective from 10 June 2018.

## 1.5 Demographic Trends

From a long-run perspective, the population of the Czech Republic has been steadily and slightly rising. At the end of 2017, 10.610 million people lived in the Czech Republic. Its population increased by 31.2 thousand persons during 2017, i.e. by 0.3%.

This increase was mainly due to a **positive net migration** of 28.3 thousand people with a YoY increase of 8.2 thousand. The migration balance reached the highest value since 2009. While 46.0 thousand persons moved from abroad, 17.7 thousand left the Czech Republic. The highest net migration balance was recorded with citizens of Ukraine (7.7 thousand) and Slovakia (4.4 thousand).

**Natural increase** in the Czech population was 3.0 thousand persons. The number of live births increased in YoY terms for the fourth time in a row in 2017. A total of 114.4 thousand children were born alive, which was 1.7 thousand more YoY and the most in the last seven years. According to preliminary calculations, the total fertility rate rose to 1.67 children per woman in 2017. Higher value of fertility was last recorded in 1992.

According to preliminary data, 111.4 thousand people died in 2017, 3.6 thousand more than in the previous year. Apparently, this increase is partially related to the influenza outbreak at the beginning of the year.

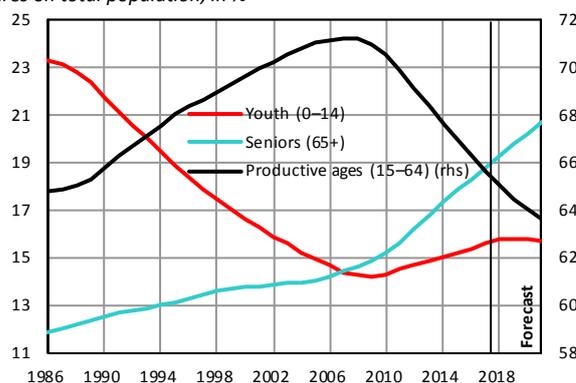
Population development is much more favourable than anticipated in the high scenario of the Czech Statistical Office's 2013 Demographic Projection, on which the assumptions of the Macroeconomic Forecast are based. There is a significant difference in the birth rate, where the number of births in 2017 exceeded the projected

value by 15 thousand, i.e. almost by 15%. The total fertility rate, as indicated above, exceeded 1.67 children compared to the projected 1.46. The causes of such difference cannot be clearly determined; the impact of the favourable economic situation is likely very significant. The developments of the death rate and cross-border migration roughly correspond to the projected values.

As regards the **age structure** of the population, seniors over 64 years are the group where there are the biggest increases, while the working-age population is shrinking.

**Graph 1.5.1: Age Groups**

shares on total population, in %



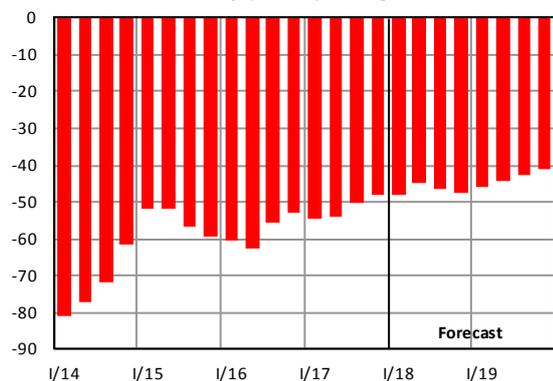
Source: CZSO. Calculations of the MoF.

The increase in the number of **old-age pensioners** is lower than would correspond to demographic development and postponement of the statutory retirement age, probably as a result of the economic boom. At the end of 2017, a total of 2.403 million old-age pensioners

were clients of the pension system, i.e. 22.7% of the Czech population.

### Graph 1.5.2: Population Aged 15–64

based on LFS, YoY increases of quarterly averages, in thousands



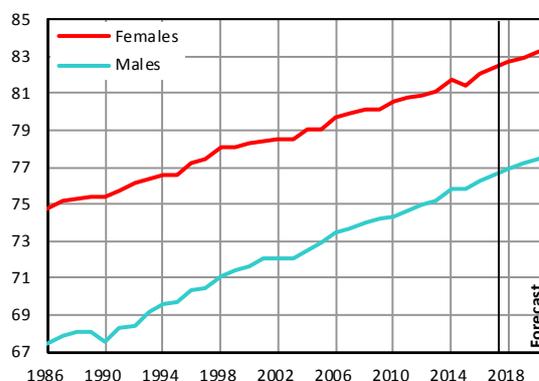
Source: CZSO. Calculations of the MoF.

The YoY increase was only 8 thousand persons, i.e. 0.3%. As the increasing number of old-age pensioners falls be-

hind the employment growth, the effective dependency ratio (see Graph 1.5.4) has markedly declined by 2.2 pp since 2012, which is one of the factors contributing to the improvement of the pensions account balance.

### Graph 1.5.3: Life Expectancy at Birth

in years



Source: CZSO.

### Table 1.5.1: Demographics

in thousands of persons (unless stated otherwise)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
							Forecast	Forecast	Outlook	Outlook
<b>Population (as of 1 January)</b>	<b>10 505</b>	<b>10 516</b>	<b>10 512</b>	<b>10 538</b>	<b>10 554</b>	<b>10 579</b>	<b>10 610</b>	<b>10 623</b>	<b>10 635</b>	<b>10 645</b>
growth in %	0.2	0.1	0.0	0.2	0.1	0.2	0.3	0.1	0.1	0.1
0–14 years	<b>1 541</b>	<b>1 560</b>	<b>1 577</b>	<b>1 601</b>	<b>1 624</b>	<b>1 647</b>	<b>1 670</b>	<b>1 675</b>	<b>1 675</b>	<b>1 668</b>
growth in %	1.3	1.2	1.1	1.5	1.4	1.5	1.4	0.3	0.0	-0.4
15–64 years	<b>7 263</b>	<b>7 188</b>	<b>7 109</b>	<b>7 057</b>	<b>6 998</b>	<b>6 943</b>	<b>6 897</b>	<b>6 850</b>	<b>6 808</b>	<b>6 774</b>
growth in %	-0.9	-1.0	-1.1	-0.7	-0.8	-0.8	-0.7	-0.7	-0.6	-0.5
65 and more years	<b>1 701</b>	<b>1 768</b>	<b>1 826</b>	<b>1 880</b>	<b>1 932</b>	<b>1 989</b>	<b>2 043</b>	<b>2 098</b>	<b>2 151</b>	<b>2 203</b>
growth in %	3.9	3.9	3.3	3.0	2.8	2.9	2.7	2.7	2.5	2.4
<b>Old-age pensioners (as of 1 January)<sup>1)</sup></b>	<b>2 340</b>	<b>2 341</b>	<b>2 340</b>	<b>2 355</b>	<b>2 377</b>	<b>2 395</b>	<b>2 403</b>	<b>2 419</b>	<b>2 433</b>	<b>2 443</b>
growth in %	3.5	0.0	0.0	0.6	0.9	0.8	0.3	0.6	0.6	0.4
<b>Old-age dependency ratios (as of 1 January, in %)</b>										
Demographic <sup>2)</sup>	<b>23.4</b>	<b>24.6</b>	<b>25.7</b>	<b>26.6</b>	<b>27.6</b>	<b>28.6</b>	<b>29.6</b>	<b>30.6</b>	<b>31.6</b>	<b>32.5</b>
Under current legislation <sup>3)</sup>	<b>37.8</b>	<b>38.3</b>	<b>38.8</b>	<b>39.3</b>	<b>39.8</b>	<b>40.1</b>	<b>40.2</b>	<b>40.6</b>	<b>40.9</b>	<b>41.1</b>
Effective <sup>4)</sup>	<b>47.9</b>	<b>47.6</b>	<b>47.2</b>	<b>46.9</b>	<b>46.8</b>	<b>46.2</b>	<b>45.7</b>	<b>45.9</b>	<b>46.1</b>	<b>46.2</b>
<b>Fertility rate</b>	<b>1.452</b>	<b>1.456</b>	<b>1.528</b>	<b>1.570</b>	<b>1.630</b>	<b>1.670</b>	<b>1.47</b>	<b>1.47</b>	<b>1.48</b>	<b>1.48</b>
<b>Population increase</b>	<b>11</b>	<b>-4</b>	<b>26</b>	<b>16</b>	<b>25</b>	<b>31</b>	<b>13</b>	<b>12</b>	<b>10</b>	<b>9</b>
<b>Natural increase</b>	<b>0</b>	<b>-2</b>	<b>4</b>	<b>0</b>	<b>5</b>	<b>3</b>	<b>-6</b>	<b>-8</b>	<b>-9</b>	<b>-11</b>
Live births	109	107	110	111	113	114	98	96	95	93
Deaths	108	109	106	111	108	111	104	104	104	104
<b>Net migration</b>	<b>10</b>	<b>-1</b>	<b>22</b>	<b>16</b>	<b>20</b>	<b>28</b>	<b>19</b>	<b>20</b>	<b>20</b>	<b>20</b>
Immigration	30	30	42	35	38	46	.	.	.	.
Emigration	20	31	20	19	17	18	.	.	.	.

<sup>1)</sup> In 2010 disability pensions of pensioners over 64 were transferred into old-age pensions.

<sup>2)</sup> Demographic dependency: ratio of people in senior ages (65 and more) to people in productive age (15–64).

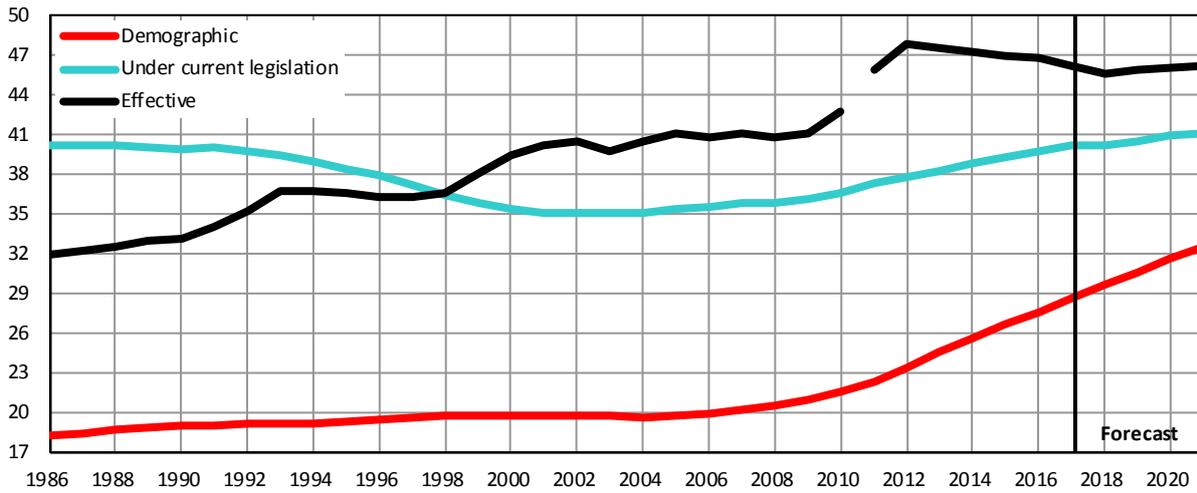
<sup>3)</sup> Dependency under current legislation: ratio of people above the official retirement age to the people over 19 below the official retirement age.

<sup>4)</sup> Effective dependency: ratio of old-age pensioners to working people (LFS methodology).

Source: Czech Social Security Administration, CZSO. Calculations of the MoF.

### Graph 1.5.4: Dependency Ratios

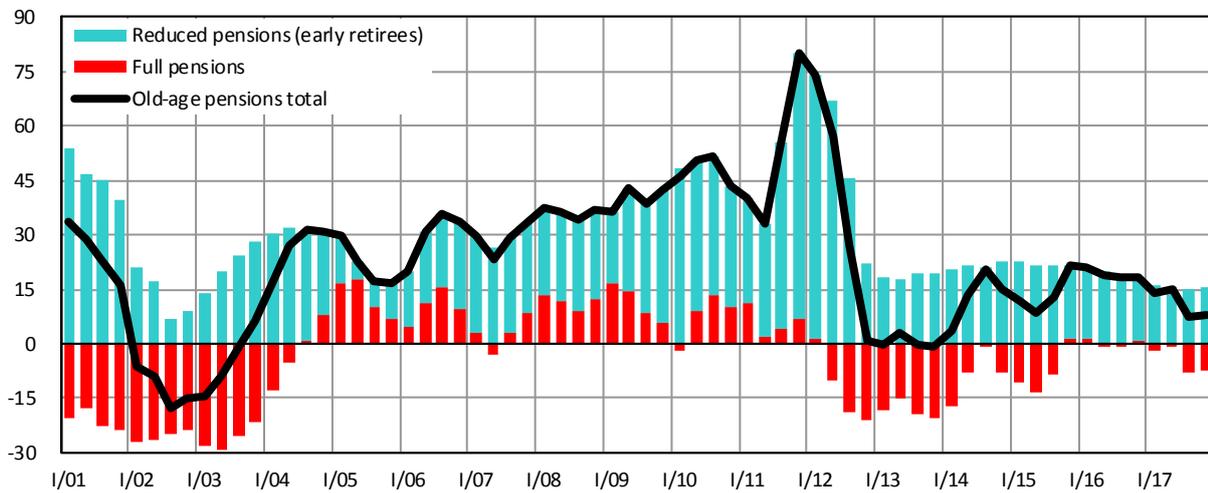
As of January 1, in %, inconsistent between 2010 and 2011 due to transfer of disability pensions to old-age pensions for people over 64 years



Source: CZSO. Calculations of the MoF.

### Graph 1.5.5: Old-Age Pensioners

absolute increase over a year in thousands of persons



Note: Adjusted for the transfer of disability pensions to old-age pensions for people over 64 years in 2010.

Source: Czech Social Security Administration, CZSO. Calculations of the MoF.

## 2 Economic Cycle

### 2.1 Position within the Economic Cycle

In the fourth quarter of 2017, the **positive output gap** reached 1.9% of the potential output (see Graph 2.1.1), i.e. a similar level to the previous two quarters. Given the forecast of economic growth and assumed developments of potential output, the output gap should hover above 2% in the coming period.

The **situation in the labour market**, which increasingly shows symptoms of overheating (see Chapter 3.3), reflects the positive output gap most clearly. The unemployment rate (LFS) was 2.4% in the fourth quarter of 2017. That is a record low not only in the history of the market economy in the CR but also a value that has not been recorded in the EU in the past 16 years. The number of job vacancies (according to the data of the Ministry of Labour and Social Affairs) has been dramatically growing and it has already exceeded the highs from the peak of the previous cycle in 2008 by almost three fifths. It is difficult to find new employees in many professions and regions, and the lack of employees is becoming a visible barrier to an extensive economic growth.

Since the beginning of 2016 the YoY **potential output growth** has stabilized at approximately 2.8%. That is a slightly better result compared to the long-term average growth of gross value added (and also of potential output) of 2.6%.

The main driver of potential growth and its acceleration is **total factor productivity**. In the fourth quarter of 2017, the contribution of its trend component was 2.3 pp.

**Labour supply** is being affected by a long-lasting decrease in the working-age population (15–64 years), caused by the process of population ageing (see Chapter 1.5). Since the end of 2014, **demographic development** has been constantly slowing down the potential output growth by 0.4 pp. However, the negative impact of population ageing on the labour supply is completely eliminated by **rising participation rate**. Structural factors – an increase in the number of inhabitants in age groups with naturally high participation and an increase in the retirement age (both statutory and effective) – as well as higher supply of jobs are predominating here. In the fourth quarter of 2017, the contribution of the participation rate to potential output growth reached 0.6 pp.

An acceleration in the gross fixed capital formation growth in the course of 2017 led to an increase in the contribution of **capital stock** to 0.6 pp in the fourth quarter of 2017.

From a long-run perspective, the regular **average working time** is shortening in the Czech Republic, which brings the Czech Republic closer to developed economies. In the fourth quarter of 2017, the contribution of the number of hours usually worked was –0.2 pp.

**Table 2.1.1: Output Gap and Potential Product**

		2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
<b>Output gap</b>	%	3.6	-3.8	-2.0	-0.7	-2.4	-4.0	-2.2	0.2	-0.2	1.4
<b>Potential product</b> <sup>1)</sup>	growth in %	3.3	2.0	0.8	0.7	0.9	1.2	1.4	2.3	2.8	2.8
<b>Contributions</b>											
Trend total factor productivity	pp	1.9	1.1	0.6	0.4	0.4	0.7	1.3	1.7	2.0	2.2
Fixed assets	pp	1.2	0.8	0.6	0.6	0.5	0.4	0.4	0.6	0.6	0.5
Demography <sup>2)</sup>	pp	0.3	0.1	-0.2	-0.4	-0.5	-0.5	-0.5	-0.4	-0.4	-0.4
Participation rate	pp	0.0	0.3	0.1	0.3	0.8	1.0	0.5	0.5	0.7	0.7
Usually worked hours	pp	-0.1	-0.3	-0.3	-0.2	-0.3	-0.3	-0.2	-0.1	-0.1	-0.2

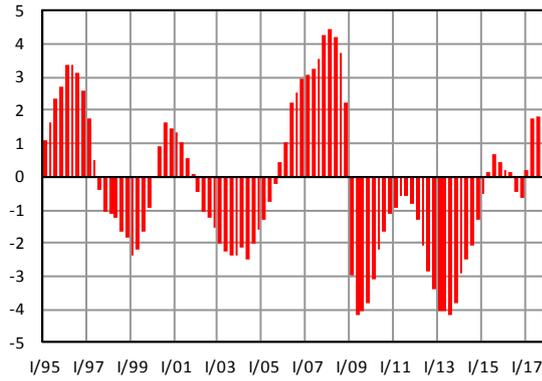
<sup>1)</sup> Based on gross value added.

<sup>2)</sup> Contribution of growth of working-age population (15–64 years).

Source: CZSO. Calculations of the MoF.

**Graph 2.1.1: Output Gap**

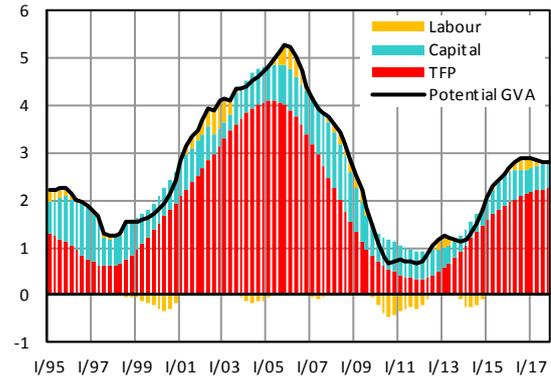
*in % of potential product*



Source: CZSO. Calculations of the MoF.

**Graph 2.1.2: Potential Product**

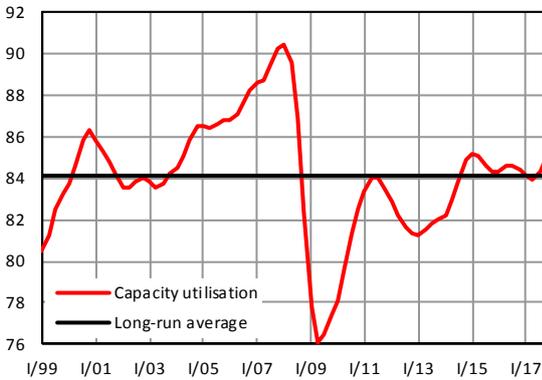
*YoY growth rate in %, contributions in percentage points*



Source: CZSO. Calculations of the MoF.

**Graph 2.1.3: Capacity Utilisation in Industry**

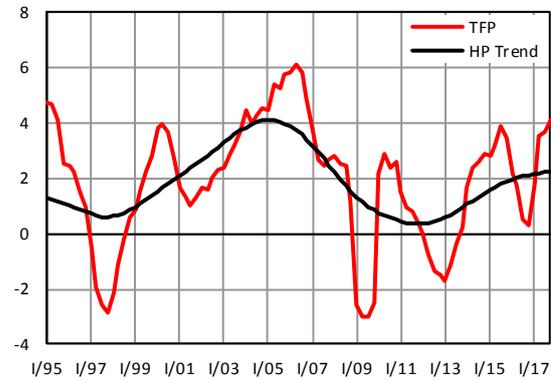
*smoothed by Hodrick-Prescott filter, in %*



Source: CZSO.

**Graph 2.1.4: Total Factor Productivity**

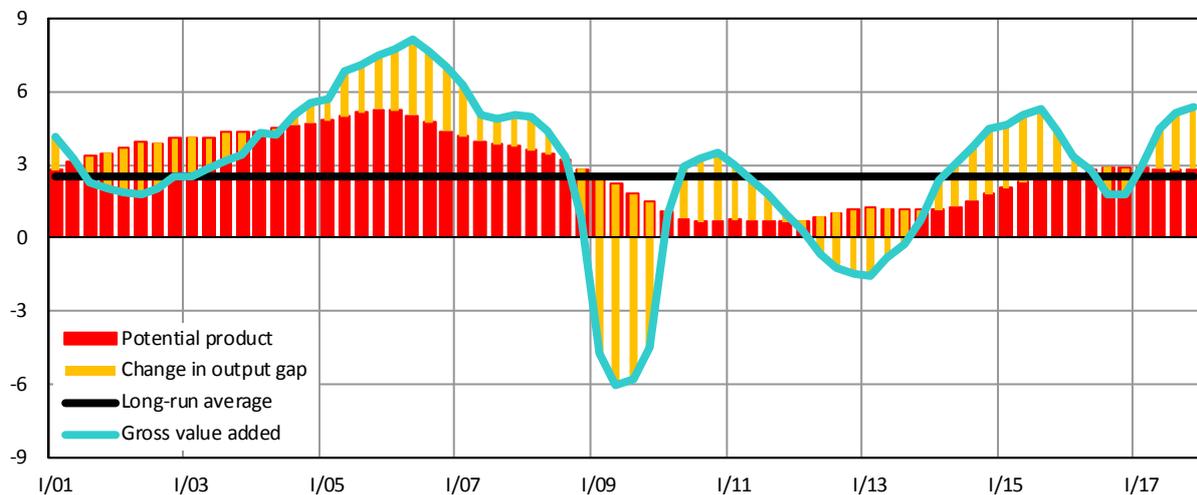
*YoY growth rate, in %*



Source: CZSO. Calculations of the MoF.

**Graph 2.1.5: Decomposition of the Growth in Gross Value Added – Business Cycle Perspective**

*YoY growth rate in %, contributions in percentage points*



Source: CZSO. Calculations of the MoF.

## 2.2 Business Cycle Indicators

The industrial confidence indicator decreased in the first quarter of 2018, indicating a likely moderate slowdown in the YoY dynamics of gross value added in industry.

Conversely, the confidence indicator in construction increased again significantly. That indicates a continued recovery of the gross value added, although the correlation between the developments of confidence and of the gross value added in construction is very low (see Graph 2.2.2).

Confidence in trade and services increased in the first quarter of 2018, which rather points to a slight acceleration of the YoY growth in gross value added in this sector.

The consumer confidence indicator increased significantly in the first quarter of 2018, reaching a record high (the

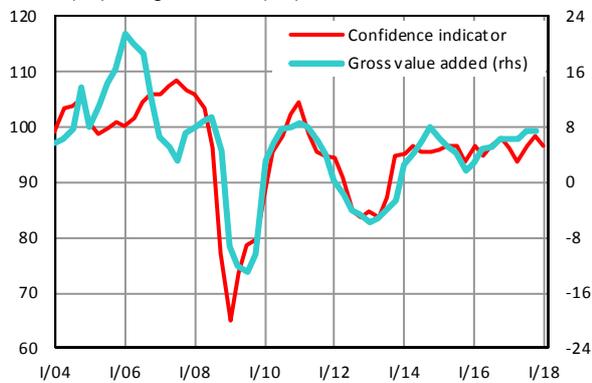
indicator has been monitored since 1998). Consumer confidence indicates an increase in the growth dynamics of household consumption in the first half of 2018 as the developments of the confidence indicator are 1–2 quarters ahead.

As a result, the composite confidence indicator signals, thanks to the strengthening of most of its components, an acceleration of the YoY growth in gross value added in the first quarter of 2018.

The composite leading indicator started approaching the output gap level at the end of 2017, and continued so to a greater extent also in early 2018. A slight increase in the output gap is thus likely signalled for the first half of 2018.

**Graph 2.2.1: Confidence and GVA in Industry**

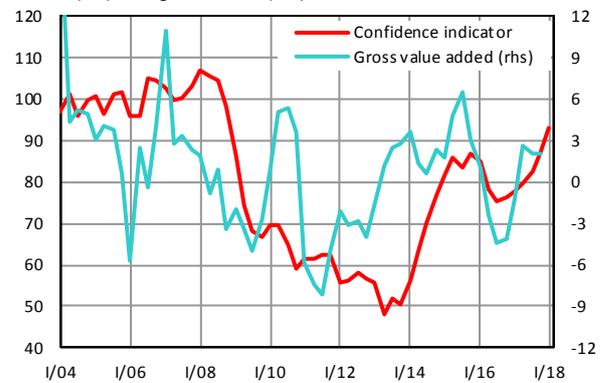
2005=100 (lhs), YoY growth in % (rhs)



Source: CZSO.

**Graph 2.2.2: Confidence and GVA in Construction**

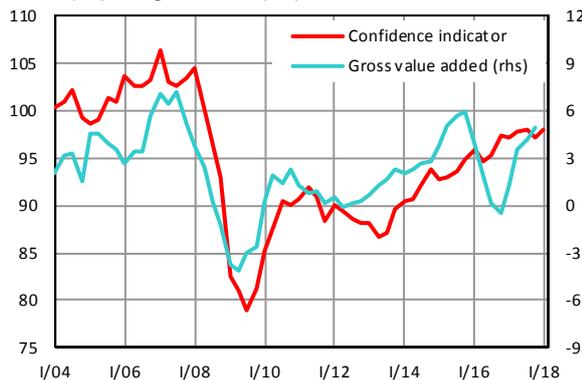
2005=100 (lhs), YoY growth in % (rhs)



Source: CZSO.

**Graph 2.2.3: Confidence and GVA in Trade and Services**

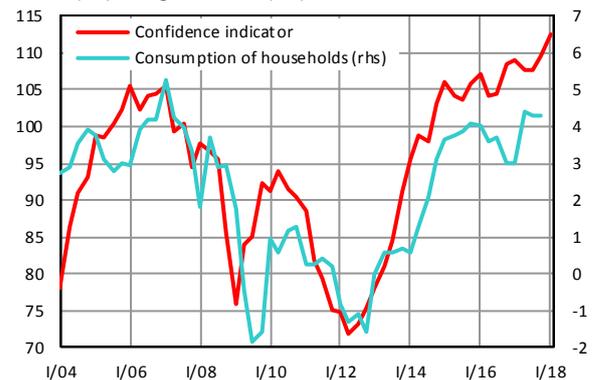
2005=100 (lhs), YoY growth in % (rhs)



Source: CZSO. Calculations of the MoF.

**Graph 2.2.4: Consumer Confidence and Consumption**

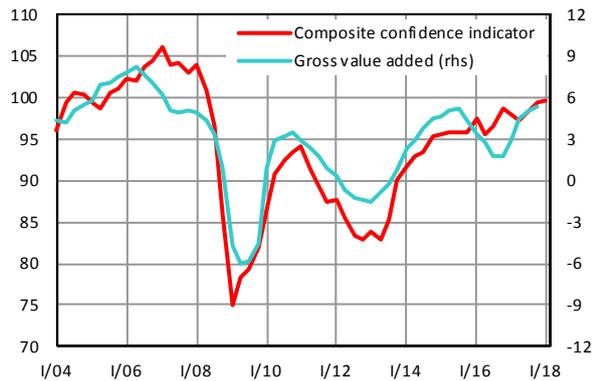
2005=100 (lhs), YoY growth in % (rhs)



Source: CZSO.

### Graph 2.2.5: Composite Confidence Indicator and GVA

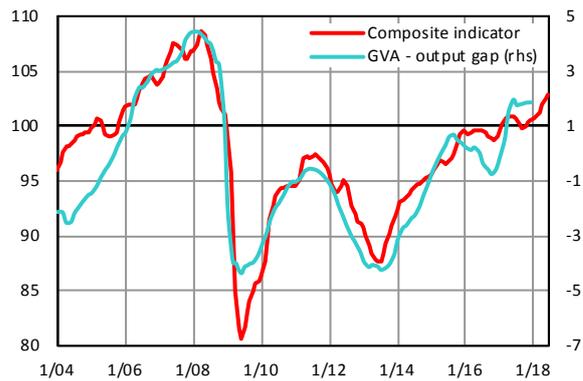
2005=100 (lhs), YoY growth in % (rhs)



Source: CZSO.

### Graph 2.2.6: Composite Leading Indicator

2005=100 (lhs), in % of GVA (rhs)



Note: Synchronized with the output gap (based on GVA) derived from the Cobb-Douglas production function (see Chapter 2.1), on a monthly basis.

Source: CZSO. Calculations of the MoF.

## 3 Forecast of Macroeconomic Developments in the CR

### 3.1 Economic Output

#### 3.1.1 GDP in the Fourth Quarter of 2017

Economic output measured by real GDP increased by 5.5% YoY (*versus 5.1%*) in the fourth quarter of 2017, while seasonally adjusted GDP rose by 0.8% QoQ (*versus 0.7%*). The QoQ growth was predominantly driven by manufacturing. For the whole of 2017, the GDP was thus up by 4.4% (*versus 4.3%*), and after working day adjustment by 4.6% (*versus 4.5%*).

The YoY increase in GDP in the fourth quarter of 2017 reflected mainly the growing domestic demand. The main growth drivers were final consumption expenditures of households and investment activity. With the growth rates of both exports and imports having increased, the contribution of the balance of foreign trade with goods and services was marginally positive.

The increase in household consumption was due to rising disposable income and unprecedentedly high consumer confidence. Final consumption expenditures of households were also supported by a YoY decrease in the savings rate. The most dynamically growing component of household consumption were expenditures on non-durable goods; however, expenditures on semi-durable and durable goods also increased significantly, which suggests that households are optimistic about their future economic situation and economic developments. Household consumption increased by 4.3% (*versus 4.4%*) in real terms. General government consumption rose by 1.5% (*versus 1.9%*).

Following a decline in 2016, the growth in gross fixed capital formation accelerated further to 7.8% (*versus 8.2%*). Investments in information and communication technologies and other machinery and equipment, as well as in non-residential buildings and structures and transport equipment were significant contributors to the increase. The strengthening of investment activity was driven by continued growth of private investments and restored investments of the general government sector, which were supported by co-financing from EU funds (see Graph 3.1.7). Considering the markedly positive YoY contribution of change in inventories, the gross capital formation increased more than investments in fixed capital, by 11.5% (*versus 8.5%*).

Thanks to favourable developments of export markets and improved export performance, the YoY growth in exports of goods and services significantly accelerated in comparison with the same quarter of 2016. Total exports thus rose by 7.5% in the fourth quarter of 2017 (*versus 5.9%*). Imports of goods and services increased by 8.1% (*versus 6.0%*). The stronger dynamics of imports reflect-

ed, in particular, the acceleration in exports and the recovery of import-intensive investment activity.

A higher decrease in import prices compared to export prices resulted in an improvement in the terms of trade of 0.3% (*versus 0.0%*). The trading gain resulting from foreign trade brought about a situation where real gross domestic income, which unlike GDP includes this factor, increased by 5.7% YoY (*versus 5.1%*).

Gross operating surplus grew by 6.5% (*versus 6.6%*), compensation of employees increased by 9.0% (*versus 8.6%*) and net taxes on production were up by 10.9% YoY (*versus 3.3%*). As a result, nominal GDP recorded growth of 8.0% (*versus 7.1%*). The strong growth in compensation of employees, which exceeded GDP dynamics in 2016 and 2017, thus led to a further shift in the distribution of the created income in favour of the production factor of labour.

#### 3.1.2 Estimate for the First Quarter of 2018

We estimate that real GDP rose by 4.0% YoY (*versus 3.9%*) and by 1.0% QoQ (*versus 0.9%*) in the first quarter of 2018. The expected increase in the QoQ dynamics of GDP reflects the data on the development of the economy in the first quarter of 2018 available as of the cut-off date of the Forecast (industrial and construction production, sales in retail and in services, confidence indicators).

We believe that the GDP growth was exclusively due to the growth in domestic demand. As a result of rising disposable income, high consumer confidence and declining savings rate, final consumption expenditures of households could have increased by 4.1% (*versus 3.9%*), while consumption of the general government sector could have risen by 1.9% (*versus 1.8%*). According to our estimates, gross capital formation was up by 10.9% (*versus 7.9%*) due to growth in investments in fixed capital and the change in inventories.

Foreign trade probably weighed on GDP dynamics, mainly due to a significant increase in import-intensive investment demand. We estimate that exports of goods and services increased by 3.3% (*versus 3.1%*) and that imports rose by 4.3% (*versus 3.5%*) in relation to the development of domestic demand and exports.

#### 3.1.3 Forecast for the Years 2018 and 2019

In 2018, economic growth should be driven solely by domestic demand led by strong final consumption expenditures of households and investment activity of firms and the general government sector. GDP growth should also be strengthened by the general government consumption. The balance of foreign trade should have

a slightly negative effect on GDP dynamics. We expect real GDP to grow by 3.6% (*versus* 3.4%) in 2018 and by 3.3% (*versus* 2.6%) in 2019.

Household consumption will be supported by growing real disposable income and declining savings rate. In 2018, the development of household consumption should positively reflect a number of discretionary changes in the social area, the dynamics of consumer loans and consumers' optimistic expectations (see Chapter 2.2). In 2019, private consumption will also be supported by pending changes to the pension system. Household consumption could thus increase by 4.3% (*versus* 3.7%) in 2018 and by 4.1% (*versus* 2.7%) in 2019.

We expect the general government consumption to increase by 1.9% (*versus* 1.8%) in 2018 and by 2.0% (*versus* 1.5%) in 2019. The main factor of growth in the general government consumption in 2018 will be an increase in social security benefits in kind, based mainly on health insurance plans and the medium-term outlook of health insurance companies, and an increase in expenditures on the purchase of goods and services with a contribution from gradually starting current grants from EU funds. Increasing number of employees should play a relatively smaller role in the real growth of general government consumption.

The gross fixed capital formation in 2018 should grow not only due to private investments but also due to investments by the general government sector. Private investments are stimulated by growing gross operating surplus, the economic boom abroad, low interest rates, and slightly above-average capacity utilization in manu-

facturing. Also, the increasing lack of employees could motivate businesses to invest in order to increase labour productivity. Conversely, certain risks in the external environment could hamper private investments. In the case of investments of the general government sector, we expect stable growth in investment expenditures financed from national resources in both these years. Investment activity in 2018 and 2019 should be supported by a gradual start of projects co-financed by the EU funds under the 2014–2020 financial perspective. The gross fixed capital formation could thus increase by 5.7% in 2018 (*versus* 4.1%) and by 4.4% in 2019 (*versus* 3.4%) with a positive contribution of government and especially private investments.

We assume that the contribution of change in inventories to GDP growth will be zero in 2018 and 2019. Gross capital formation should thus increase by 5.4% (*versus* 4.1%) in 2018, and its growth should slow down to 4.0% (*versus* 3.5%) in 2019.

We expect that exports of goods and services will grow by 5.2% (*versus* 5.4%) in 2018 and by 4.9% (*versus* 5.0%) in 2019. The dynamics of exports of goods and services reflects mainly the expected export market growth (see Chapter 3.4), and to a lesser extent also an increase in export performance. On the side of imports of goods and services, we expect influence of the growth in imports and gross domestic expenditures, especially import-intensive investment demand. Hence, imports will probably grow by 5.9% (*versus* 5.6%) in 2018 and by 5.4% (*unchanged*) in 2019.

**Table 3.1.1: Real GDP by Type of Expenditure – yearly***chained volumes, reference year 2010*

		2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
								<i>Forecast</i>	<i>Forecast</i>	<i>Outlook</i>	<i>Outlook</i>
<b>Gross domestic product</b>	<i>bill. CZK 2010</i>	4 001	3 981	4 089	4 307	4 418	4 612	4 780	4 939	5 068	5 191
	<i>growth in %</i>	-0.8	-0.5	2.7	5.3	2.6	4.4	3.6	3.3	2.6	2.4
	<i>growth in %<sup>1)</sup></i>	-0.7	-0.5	2.7	5.4	2.5	4.6	3.6	3.2	2.6	2.4
<b>Private consumption expenditure<sup>2)</sup></b>	<i>bill. CZK 2010</i>	1 921	1 931	1 966	2 038	2 112	2 196	2 291	2 384	2 455	2 517
	<i>growth in %</i>	-1.2	0.5	1.8	3.7	3.6	4.0	4.3	4.1	2.9	2.6
<b>Government consumption exp.</b>	<i>bill. CZK 2010</i>	783	803	812	827	844	857	873	890	906	922
	<i>growth in %</i>	-2.0	2.5	1.1	1.9	2.0	1.5	1.9	2.0	1.8	1.8
<b>Gross capital formation</b>	<i>bill. CZK 2010</i>	1 051	997	1 083	1 223	1 195	1 252	1 320	1 373	1 410	1 447
	<i>growth in %</i>	-3.9	-5.1	8.6	13.0	-2.3	4.7	5.4	4.0	2.7	2.6
Gross fixed capital formation	<i>bill. CZK 2010</i>	1 042	1 016	1 056	1 164	1 137	1 199	1 268	1 323	1 362	1 401
	<i>growth in %</i>	-3.1	-2.5	3.9	10.2	-2.3	5.4	5.7	4.4	3.0	2.8
Change in stocks and valuables	<i>bill. CZK 2010</i>	9	-19	26	59	58	53	52	50	48	46
<b>Exports of goods and services</b>	<i>bill. CZK 2010</i>	2 978	2 984	3 242	3 437	3 593	3 826	4 023	4 220	4 412	4 606
	<i>growth in %</i>	4.3	0.2	8.7	6.0	4.5	6.5	5.2	4.9	4.5	4.4
<b>Imports of goods and services</b>	<i>bill. CZK 2010</i>	2 732	2 734	3 008	3 212	3 320	3 513	3 722	3 924	4 111	4 297
	<i>growth in %</i>	2.7	0.1	10.1	6.8	3.4	5.8	5.9	5.4	4.8	4.5
<b>Gross domestic expenditure</b>	<i>bill. CZK 2010</i>	3 756	3 733	3 860	4 087	4 150	4 303	4 481	4 643	4 766	4 881
	<i>growth in %</i>	-2.1	-0.6	3.4	5.9	1.5	3.7	4.1	3.6	2.6	2.4
<b>Methodological discrepancy<sup>3)</sup></b>	<i>bill. CZK 2010</i>	-1	-1	-4	-7	-5	-5	-5	-4	-4	-3
<b>Real gross domestic income</b>	<i>bill. CZK 2010</i>	3 942	3 956	4 112	4 344	4 493	4 655	4 830	4 993	5 129	5 254
	<i>growth in %</i>	-1.2	0.4	3.9	5.6	3.4	3.6	3.8	3.4	2.7	2.4
<b>Contributions to GDP growth<sup>4)</sup></b>											
<b>Gross domestic expenditure</b>	<i>pp</i>	-2.1	-0.6	3.2	5.5	1.4	3.4	3.8	3.4	2.5	2.3
Consumption	<i>pp</i>	-1.0	0.8	1.1	2.2	2.1	2.2	2.4	2.3	1.8	1.6
Household expenditure	<i>pp</i>	-0.6	0.3	0.9	1.8	1.7	1.9	2.0	1.9	1.4	1.2
Government expenditure	<i>pp</i>	-0.4	0.5	0.2	0.4	0.4	0.3	0.4	0.4	0.3	0.3
Gross capital formation	<i>pp</i>	-1.1	-1.3	2.1	3.4	-0.6	1.2	1.4	1.1	0.7	0.7
Gross fixed capital formation	<i>pp</i>	-0.8	-0.6	1.0	2.6	-0.6	1.4	1.4	1.1	0.8	0.7
Change in stocks	<i>pp</i>	-0.2	-0.7	1.1	0.8	0.0	-0.1	0.0	0.0	0.0	0.0
<b>Foreign balance</b>	<i>pp</i>	1.3	0.1	-0.5	-0.2	1.2	1.0	-0.2	-0.1	0.1	0.2
External balance of goods	<i>pp</i>	1.4	0.1	-0.1	-1.1	0.8	0.7	-0.2	-0.1	0.0	0.1
External balance of services	<i>pp</i>	-0.1	0.0	-0.4	0.9	0.4	0.2	0.0	0.1	0.1	0.1
<b>Gross value added</b>	<i>bill. CZK 2010</i>	3 624	3 606	3 729	3 905	4 004	4 175	.	.	.	.
	<i>growth in %</i>	-0.8	-0.5	3.4	4.7	2.5	4.3	.	.	.	.
<b>Net taxes and subsidies on products</b>	<i>bill. CZK 2010</i>	376	375	363	402	415	438	.	.	.	.

<sup>1)</sup> From working day adjusted data.<sup>2)</sup> The consumption of non-profit institutions serving households (NPISH) is included in the private consumption.<sup>3)</sup> Deterministic impact of using prices and structure of the previous year for calculation of y-o-y growth.<sup>4)</sup> Calculated on the basis of prices and structure of the previous year with perfectly additive contributions.

Source: CZSO. Calculations of the MoF.

**Table 3.1.2: Real GDP by Type of Expenditure – quarterly**

chained volumes, reference year 2010

		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
		<i>Prelim.</i>	<i>Prelim.</i>	<i>Prelim.</i>	<i>Prelim.</i>	<i>Estimate</i>	<i>Forecast</i>	<i>Forecast</i>	<i>Forecast</i>
<b>Gross domestic product</b>	<i>bill. CZK 2010</i>	1 073	1 164	1 173	1 202	1 120	1 206	1 212	1 243
	<i>growth in %</i>	<b>4.0</b>	<b>3.3</b>	<b>4.8</b>	<b>5.5</b>	<b>4.3</b>	<b>3.6</b>	<b>3.3</b>	<b>3.4</b>
	<i>growth in %<sup>1)</sup></i>	<b>3.0</b>	<b>4.6</b>	<b>5.2</b>	<b>5.5</b>	<b>5.0</b>	<b>3.3</b>	<b>3.2</b>	<b>3.0</b>
	<i>QoQ in %<sup>1)</sup></i>	<b>1.5</b>	<b>2.4</b>	<b>0.7</b>	<b>0.8</b>	<b>1.0</b>	<b>0.8</b>	<b>0.6</b>	<b>0.6</b>
<b>Private consumption expenditure<sup>2)</sup></b>	<i>bill. CZK 2010</i>	519	548	556	573	541	571	580	599
	<i>growth in %</i>	<b>3.7</b>	<b>3.9</b>	<b>4.1</b>	<b>4.3</b>	<b>4.1</b>	<b>4.3</b>	<b>4.3</b>	<b>4.6</b>
<b>Government consumption exp.</b>	<i>bill. CZK 2010</i>	200	210	208	240	204	214	211	244
	<i>growth in %</i>	<b>2.3</b>	<b>1.5</b>	<b>0.8</b>	<b>1.5</b>	<b>1.9</b>	<b>1.9</b>	<b>1.9</b>	<b>1.9</b>
<b>Gross capital formation</b>	<i>bill. CZK 2010</i>	249	313	352	337	276	325	365	353
	<i>growth in %</i>	<b>-1.5</b>	<b>0.6</b>	<b>7.2</b>	<b>11.5</b>	<b>10.9</b>	<b>3.8</b>	<b>3.8</b>	<b>4.5</b>
Gross fixed capital formation	<i>bill. CZK 2010</i>	261	286	309	342	276	300	326	365
	<i>growth in %</i>	<b>2.6</b>	<b>4.5</b>	<b>6.2</b>	<b>7.8</b>	<b>5.8</b>	<b>4.7</b>	<b>5.5</b>	<b>6.7</b>
Change in stocks and valuables	<i>bill. CZK 2010</i>	-12	27	43	-5	0	26	39	-13
<b>Exports of goods and services</b>	<i>bill. CZK 2010</i>	956	974	910	986	988	1 032	956	1 047
	<i>growth in %</i>	<b>7.5</b>	<b>4.4</b>	<b>6.5</b>	<b>7.5</b>	<b>3.3</b>	<b>6.0</b>	<b>5.1</b>	<b>6.1</b>
<b>Imports of goods and services</b>	<i>bill. CZK 2010</i>	851	880	849	933	887	935	899	1 001
	<i>growth in %</i>	<b>5.6</b>	<b>3.4</b>	<b>6.1</b>	<b>8.1</b>	<b>4.3</b>	<b>6.3</b>	<b>5.9</b>	<b>7.2</b>
<b>Gross domestic expenditure</b>	<i>bill. CZK 2010</i>	969	1 071	1 114	1 150	1 021	1 110	1 155	1 196
	<i>growth in %</i>	<b>2.1</b>	<b>2.4</b>	<b>4.4</b>	<b>5.7</b>	<b>5.4</b>	<b>3.7</b>	<b>3.6</b>	<b>4.0</b>
<b>Methodological discrepancy<sup>3)</sup></b>	<i>bill. CZK 2010</i>	0	-2	-3	-1	-2	-2	-2	1
<b>Real gross domestic income</b>	<i>bill. CZK 2010</i>	1 079	1 172	1 188	1 216	1 128	1 215	1 227	1 259
	<i>growth in %</i>	<b>2.3</b>	<b>1.9</b>	<b>4.3</b>	<b>5.7</b>	<b>4.5</b>	<b>3.7</b>	<b>3.3</b>	<b>3.6</b>
<b>Gross value added</b>	<i>bill. CZK 2010</i>	979	1 054	1 059	1 083	.	.	.	.
	<i>growth in %</i>	<b>4.0</b>	<b>3.0</b>	<b>4.7</b>	<b>5.3</b>	.	.	.	.
	<i>growth in %<sup>1)</sup></i>	<b>2.9</b>	<b>4.5</b>	<b>5.1</b>	<b>5.4</b>	.	.	.	.
	<i>QoQ in %<sup>1)</sup></i>	<b>1.5</b>	<b>2.2</b>	<b>0.8</b>	<b>0.8</b>	.	.	.	.
<b>Net taxes and subsidies on products</b>	<i>bill. CZK 2010</i>	95	110	114	119	.	.	.	.

<sup>1)</sup> From seasonally and working day adjusted data<sup>2)</sup> The consumption of non-profit institutions serving households (NPISH) is included in the private consumption.<sup>3)</sup> Deterministic impact of using prices and structure of the previous year for calculation of y-o-y growth.

Source: CZSO. Calculations of the MoF.

**Table 3.1.3: Nominal GDP by Type of Expenditure – yearly**

		2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
								Forecast	Forecast	Outlook	Outlook
<b>Gross domestic product</b>	bill. CZK	<b>4 060</b>	<b>4 098</b>	<b>4 314</b>	<b>4 596</b>	<b>4 773</b>	<b>5 055</b>	<b>5 320</b>	<b>5 596</b>	<b>5 840</b>	<b>6 094</b>
	growth in %	0.6	0.9	5.3	6.5	3.9	5.9	5.2	5.2	4.4	4.3
<b>Private consumption expenditure <sup>1)</sup></b>	bill. CZK	<b>1 998</b>	<b>2 025</b>	<b>2 074</b>	<b>2 152</b>	<b>2 242</b>	<b>2 388</b>	<b>2 546</b>	<b>2 701</b>	<b>2 831</b>	<b>2 955</b>
	growth in %	1.0	1.4	2.4	3.8	4.2	6.5	6.6	6.1	4.8	4.4
<b>Government consumption exp.</b>	bill. CZK	<b>804</b>	<b>826</b>	<b>849</b>	<b>883</b>	<b>917</b>	<b>969</b>	<b>1 017</b>	<b>1 076</b>	<b>1 122</b>	<b>1 170</b>
	growth in %	-1.1	2.7	2.8	4.0	3.9	5.6	5.0	5.8	4.3	4.3
<b>Gross capital formation</b>	bill. CZK	<b>1 063</b>	<b>1 011</b>	<b>1 116</b>	<b>1 285</b>	<b>1 257</b>	<b>1 334</b>	<b>1 411</b>	<b>1 476</b>	<b>1 531</b>	<b>1 592</b>
	growth in %	-2.2	-4.9	10.4	15.1	-2.1	6.1	5.7	4.6	3.7	4.0
Gross fixed capital formation	bill. CZK	<b>1 052</b>	<b>1 027</b>	<b>1 084</b>	<b>1 216</b>	<b>1 192</b>	<b>1 273</b>	<b>1 352</b>	<b>1 420</b>	<b>1 477</b>	<b>1 540</b>
	growth in %	-1.4	-2.4	5.5	12.2	-2.0	6.9	6.2	5.0	4.0	4.3
Change in stocks and valuables	bill. CZK	<b>11</b>	<b>-16</b>	<b>32</b>	<b>68</b>	<b>66</b>	<b>61</b>	<b>58</b>	<b>56</b>	<b>54</b>	<b>52</b>
<b>External balance</b>	bill. CZK	<b>195</b>	<b>236</b>	<b>275</b>	<b>276</b>	<b>357</b>	<b>364</b>	<b>347</b>	<b>343</b>	<b>356</b>	<b>377</b>
Exports of goods and services	bill. CZK	<b>3 092</b>	<b>3 150</b>	<b>3 561</b>	<b>3 725</b>	<b>3 797</b>	<b>4 007</b>	<b>4 079</b>	<b>4 271</b>	<b>4 483</b>	<b>4 705</b>
	growth in %	7.5	1.9	13.0	4.6	1.9	5.5	1.8	4.7	5.0	4.9
Imports of goods and services	bill. CZK	<b>2 897</b>	<b>2 914</b>	<b>3 286</b>	<b>3 449</b>	<b>3 439</b>	<b>3 643</b>	<b>3 732</b>	<b>3 928</b>	<b>4 127</b>	<b>4 329</b>
	growth in %	6.5	0.6	12.8	5.0	-0.3	5.9	2.4	5.3	5.1	4.9
<b>Gross national income</b>	bill. CZK	<b>3 808</b>	<b>3 854</b>	<b>4 022</b>	<b>4 285</b>	<b>4 468</b>	<b>4 770</b>	<b>5 021</b>	<b>5 287</b>	<b>5 521</b>	<b>5 765</b>
	growth in %	2.1	1.2	4.4	6.5	4.3	6.8	5.3	5.3	4.4	4.4
<b>Primary income balance</b>	bill. CZK	<b>-252</b>	<b>-245</b>	<b>-292</b>	<b>-310</b>	<b>-305</b>	<b>-285</b>	<b>-299</b>	<b>-309</b>	<b>-319</b>	<b>-329</b>

<sup>1)</sup> The consumption of non-profit institutions serving households (NPISH) is included in the private consumption.

Source: CZSO. Calculations of the MoF.

**Table 3.1.4: Nominal GDP by Type of Expenditure – quarterly**

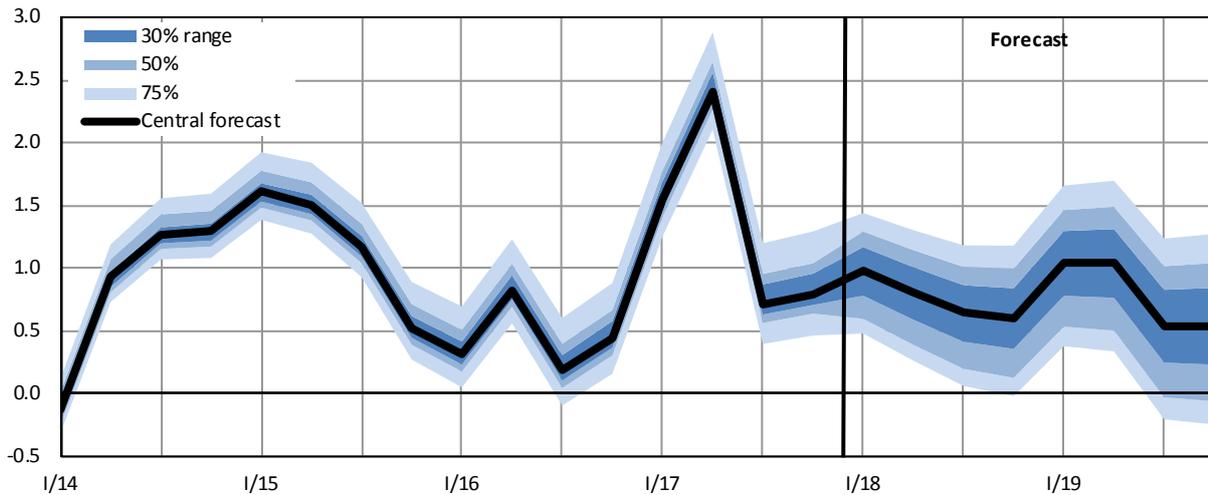
		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
		Prelim.	Prelim.	Prelim.	Prelim.	Estimate	Forecast	Forecast	Forecast
<b>Gross domestic product</b>	bill. CZK	<b>1 160</b>	<b>1 266</b>	<b>1 289</b>	<b>1 340</b>	<b>1 228</b>	<b>1 332</b>	<b>1 353</b>	<b>1 408</b>
	growth in %	4.6	4.3	6.5	8.0	5.8	5.2	5.0	5.1
<b>Private consumption expenditure <sup>1)</sup></b>	bill. CZK	<b>560</b>	<b>593</b>	<b>606</b>	<b>629</b>	<b>596</b>	<b>633</b>	<b>647</b>	<b>671</b>
	growth in %	6.1	6.1	6.6	7.2	6.3	6.8	6.6	6.6
<b>Government consumption exp.</b>	bill. CZK	<b>217</b>	<b>234</b>	<b>233</b>	<b>285</b>	<b>228</b>	<b>246</b>	<b>245</b>	<b>298</b>
	growth in %	5.5	5.4	4.9	6.5	5.2	5.3	5.1	4.3
<b>Gross capital formation</b>	bill. CZK	<b>266</b>	<b>335</b>	<b>375</b>	<b>359</b>	<b>296</b>	<b>348</b>	<b>390</b>	<b>377</b>
	growth in %	-0.2	2.8	8.9	11.9	11.2	3.8	4.1	5.3
Gross fixed capital formation	bill. CZK	<b>278</b>	<b>304</b>	<b>328</b>	<b>362</b>	<b>296</b>	<b>320</b>	<b>348</b>	<b>389</b>
	growth in %	4.3	6.3	7.7	8.6	6.2	5.0	6.0	7.4
Change in stocks and valuables	bill. CZK	<b>-12</b>	<b>31</b>	<b>47</b>	<b>-4</b>	<b>0</b>	<b>28</b>	<b>42</b>	<b>-12</b>
<b>External balance</b>	bill. CZK	<b>117</b>	<b>105</b>	<b>75</b>	<b>67</b>	<b>109</b>	<b>106</b>	<b>71</b>	<b>61</b>
Exports of goods and services	bill. CZK	<b>1 023</b>	<b>1 029</b>	<b>943</b>	<b>1 012</b>	<b>1 005</b>	<b>1 046</b>	<b>968</b>	<b>1 059</b>
	growth in %	9.0	4.7	4.5	4.0	-1.8	1.7	2.7	4.7
Imports of goods and services	bill. CZK	<b>906</b>	<b>923</b>	<b>868</b>	<b>946</b>	<b>897</b>	<b>940</b>	<b>897</b>	<b>998</b>
	growth in %	9.3	5.5	4.9	4.2	-1.0	1.8	3.4	5.5

<sup>1)</sup> The consumption of non-profit institutions serving households (NPISH) is included in the private consumption.

Source: CZSO. Calculations of the MoF.

### Graph 3.1.1: Gross Domestic Product (real)

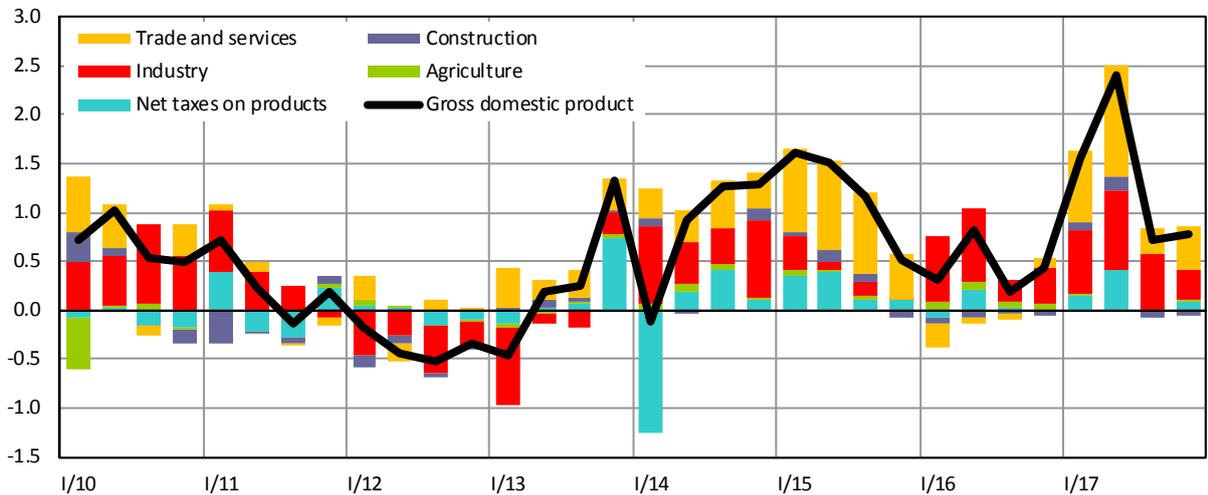
QoQ growth rate, in %, seasonally adjusted, past probability distribution reflects the actual distribution of data revisions, future probability distribution is based upon the MoF's forecasting performance



Source: CZSO. Calculations of the MoF.

### Graph 3.1.2: Resources of Gross Domestic Product

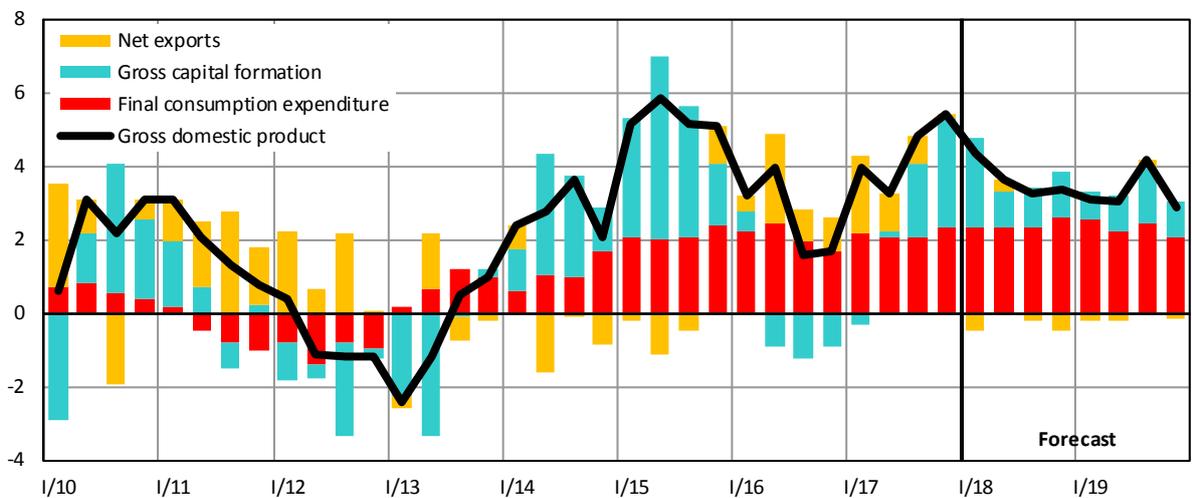
QoQ real growth rate of GDP in %, contributions of individual components in percentage points, seasonally adjusted



Source: CZSO. Calculations of the MoF.

### Graph 3.1.3: Gross Domestic Product by Type of Expenditure

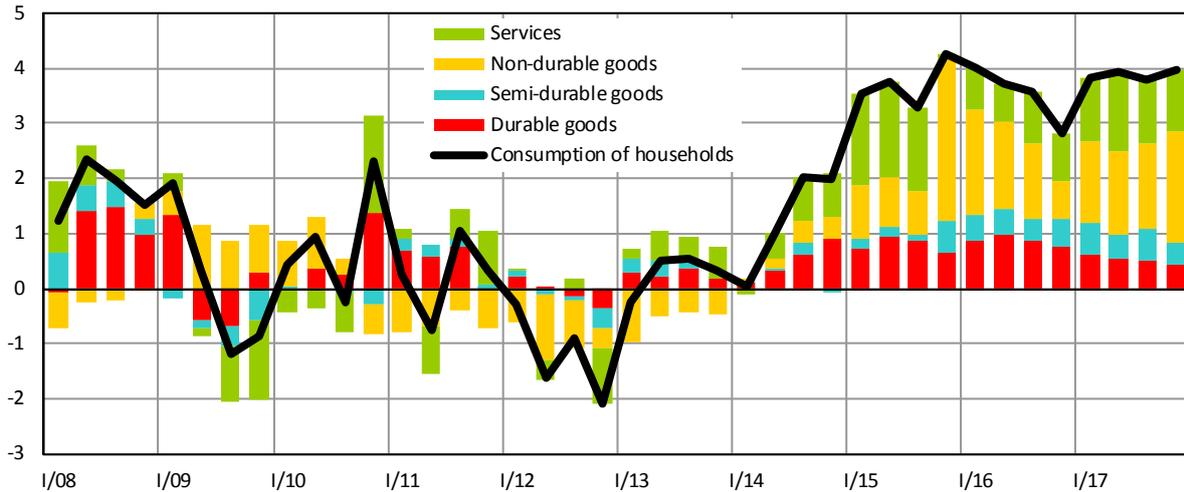
YoY real growth rate of GDP in %, contributions of individual components in percentage points



Source: CZSO. Calculations of the MoF.

### Graph 3.1.4: Consumption of Households

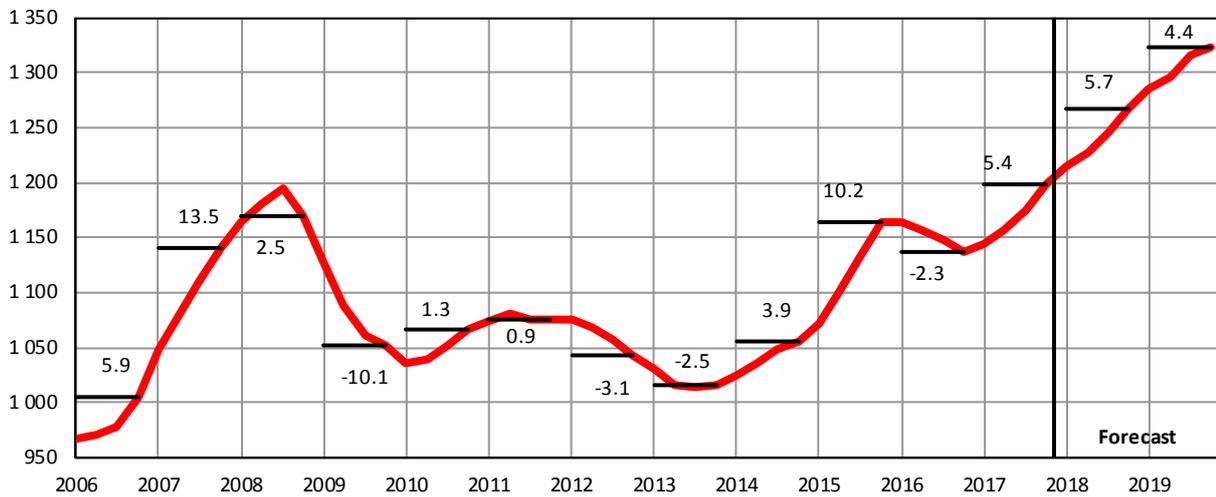
consumption of households in domestic concept, YoY real growth rate in %, contributions of individual components in percentage points



Source: CZSO. Calculations of the MoF.

### Graph 3.1.5: Gross Fixed Capital Formation

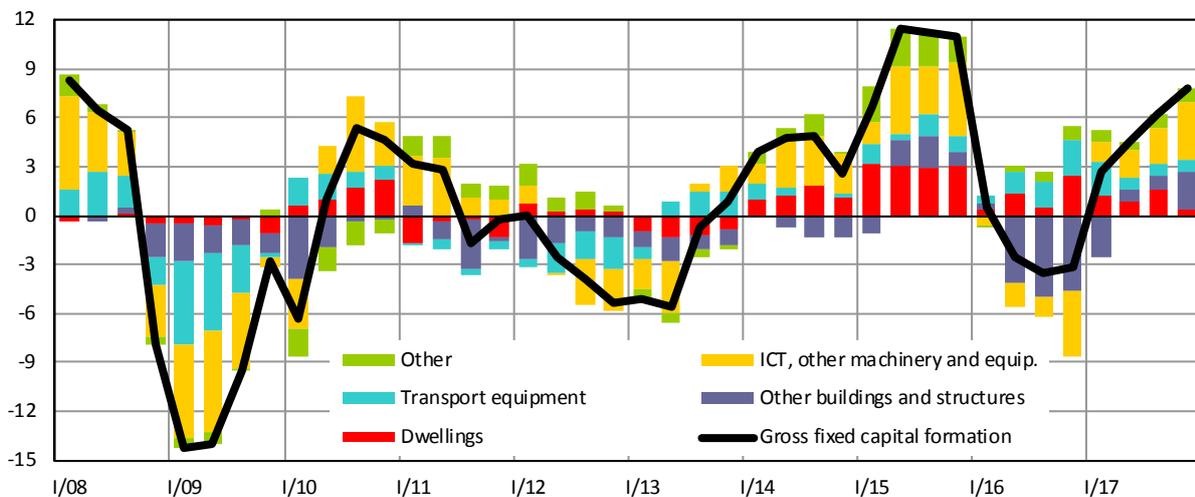
yearly moving sums, bill. CZK in const. prices of 2010, black lines with labels show the average level and growth rate in the given year



Source: CZSO. Calculations of the MoF.

### Graph 3.1.6: Gross Fixed Capital Formation by Type of Expenditure

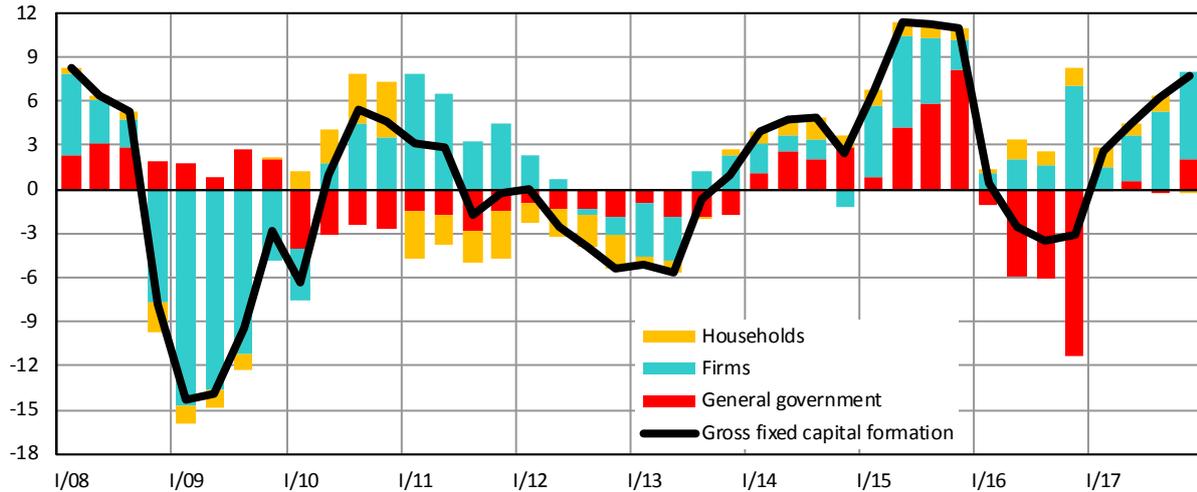
YoY real growth rate in %, contributions of individual components in percentage points



Source: CZSO. Calculations of the MoF.

### Graph 3.1.7: Gross Fixed Capital Formation by Sector

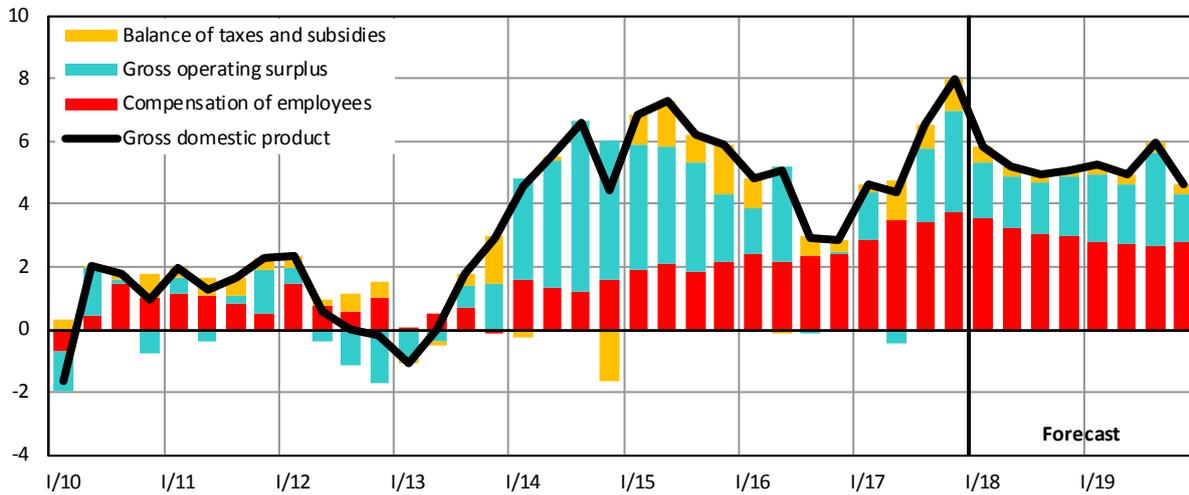
YoY real growth rate in %, contributions of individual sectors in percentage points



Source: CZSO. Calculations of the MoF.

### Graph 3.1.8: Nominal Gross Domestic Product

YoY growth rate of GDP in %, contributions of individual components in percentage points



Source: CZSO. Calculations of the MoF.

**Table 3.1.5: GDP by Type of Income – yearly**

		2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
								Forecast	Forecast	Outlook	Outlook
<b>GDP</b>	<i>bill. CZK</i>	<b>4 060</b>	<b>4 098</b>	<b>4 314</b>	<b>4 596</b>	<b>4 773</b>	<b>5 055</b>	<b>5 320</b>	<b>5 596</b>	<b>5 840</b>	<b>6 094</b>
	<i>growth in %</i>	0.6	0.9	5.3	6.5	3.9	5.9	5.2	5.2	4.4	4.3
<b>Balance of taxes and subsidies</b>	<i>bill. CZK</i>	<b>385</b>	<b>402</b>	<b>381</b>	<b>434</b>	<b>455</b>	<b>495</b>	<b>511</b>	<b>528</b>	<b>547</b>	<b>565</b>
	<i>% of GDP</i>	9.5	9.8	8.8	9.4	9.5	9.8	9.6	9.4	9.4	9.3
	<i>growth in %</i>	4.4	4.2	-5.1	13.8	4.7	8.8	3.3	3.4	3.5	3.3
Taxes on production and imports	<i>bill. CZK</i>	<b>508</b>	<b>528</b>	<b>518</b>	<b>571</b>	<b>601</b>	<b>638</b>	.	.	.	.
	<i>growth in %</i>	4.1	3.9	-1.8	10.1	5.4	6.1	.	.	.	.
Subsidies on production	<i>bill. CZK</i>	<b>123</b>	<b>126</b>	<b>137</b>	<b>137</b>	<b>147</b>	<b>143</b>	.	.	.	.
	<i>growth in %</i>	3.0	2.7	8.5	-0.1	7.5	-2.4	.	.	.	.
<b>Compensation of employees</b> <i>(domestic concept)</i>	<i>bill. CZK</i>	<b>1 665</b>	<b>1 676</b>	<b>1 735</b>	<b>1 821</b>	<b>1 929</b>	<b>2 090</b>	<b>2 251</b>	<b>2 397</b>	<b>2 529</b>	<b>2 667</b>
	<i>% of GDP</i>	41.0	40.9	40.2	39.6	40.4	41.3	42.3	42.8	43.3	43.8
	<i>growth in %</i>	2.4	0.7	3.5	5.0	5.9	8.4	7.7	6.5	5.5	5.4
Wages and salaries	<i>bill. CZK</i>	<b>1 269</b>	<b>1 275</b>	<b>1 321</b>	<b>1 384</b>	<b>1 464</b>	<b>1 586</b>	<b>1 708</b>	<b>1 819</b>	<b>1 919</b>	<b>2 024</b>
	<i>growth in %</i>	2.6	0.5	3.6	4.8	5.8	8.3	7.7	6.5	5.5	5.4
Social security contributions	<i>bill. CZK</i>	<b>396</b>	<b>402</b>	<b>414</b>	<b>437</b>	<b>464</b>	<b>504</b>	<b>543</b>	<b>578</b>	<b>610</b>	<b>643</b>
	<i>growth in %</i>	1.6	1.4	3.1	5.5	6.3	8.6	7.7	6.5	5.5	5.4
<b>Gross operating surplus</b>	<i>bill. CZK</i>	<b>2 010</b>	<b>2 020</b>	<b>2 198</b>	<b>2 341</b>	<b>2 390</b>	<b>2 470</b>	<b>2 558</b>	<b>2 671</b>	<b>2 764</b>	<b>2 862</b>
	<i>% of GDP</i>	49.5	49.3	50.9	50.9	50.1	48.9	48.1	47.7	47.3	47.0
	<i>growth in %</i>	-1.4	0.5	8.8	6.5	2.1	3.4	3.5	4.4	3.5	3.6
Consumption of capital	<i>bill. CZK</i>	<b>880</b>	<b>906</b>	<b>939</b>	<b>969</b>	<b>995</b>	<b>1 031</b>	<b>1 077</b>	<b>1 143</b>	<b>1 210</b>	<b>1 280</b>
	<i>growth in %</i>	1.8	3.0	3.6	3.2	2.7	3.6	4.5	6.1	5.9	5.8
Net operating surplus	<i>bill. CZK</i>	<b>1 130</b>	<b>1 114</b>	<b>1 259</b>	<b>1 372</b>	<b>1 395</b>	<b>1 440</b>	<b>1 481</b>	<b>1 528</b>	<b>1 554</b>	<b>1 583</b>
	<i>growth in %</i>	-3.8	-1.4	13.0	9.0	1.7	3.2	2.9	3.2	1.7	1.9

Source: CZSO. Calculations of the MoF.

**Table 3.1.6: GDP by Type of Income – quarterly**

		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
		<i>Prelim.</i>	<i>Prelim.</i>	<i>Prelim.</i>	<i>Prelim.</i>	<i>Estimate</i>	<i>Forecast</i>	<i>Forecast</i>	<i>Forecast</i>
<b>GDP</b>	<i>bill. CZK</i>	<b>1 160</b>	<b>1 266</b>	<b>1 289</b>	<b>1 340</b>	<b>1 228</b>	<b>1 332</b>	<b>1 353</b>	<b>1 408</b>
	<i>growth in %</i>	4.6	4.3	6.5	8.0	5.8	5.2	5.0	5.1
<b>Balance of taxes and subsidies</b>	<i>bill. CZK</i>	<b>103</b>	<b>128</b>	<b>136</b>	<b>128</b>	<b>109</b>	<b>132</b>	<b>139</b>	<b>131</b>
	<i>growth in %</i>	2.3	14.0	7.6	10.9	6.2	2.8	2.4	2.3
<b>Compensation of employees</b> <i>(domestic concept)</i>	<i>bill. CZK</i>	<b>493</b>	<b>519</b>	<b>518</b>	<b>560</b>	<b>534</b>	<b>559</b>	<b>558</b>	<b>600</b>
	<i>growth in %</i>	6.8	8.8	8.7	9.0	8.3	7.8	7.6	7.2
	Wages and salaries	<i>bill. CZK</i>	<b>373</b>	<b>392</b>	<b>394</b>	<b>427</b>	<b>404</b>	<b>422</b>	<b>424</b>
	<i>growth in %</i>	7.0	8.5	8.4	9.1	8.3	7.8	7.6	7.2
Social security contributions	<i>bill. CZK</i>	<b>120</b>	<b>127</b>	<b>125</b>	<b>133</b>	<b>130</b>	<b>137</b>	<b>134</b>	<b>142</b>
	<i>growth in %</i>	6.1	9.9	9.5	8.7	8.3	7.8	7.6	7.2
<b>Gross operating surplus</b>	<i>bill. CZK</i>	<b>564</b>	<b>619</b>	<b>635</b>	<b>652</b>	<b>585</b>	<b>641</b>	<b>656</b>	<b>677</b>
	<i>growth in %</i>	3.2	-0.8	4.6	6.5	3.6	3.4	3.3	3.8

Source: CZSO. Calculations of the MoF.

## 3.2 Prices

### 3.2.1 Consumer Prices

Growth in consumer prices was 1.8% YoY (*versus* 2.3%) in February 2018. Price developments in the food and non-alcoholic beverages division, where the YoY growth unexpectedly slowed down to 2.3%, contributed to a significantly lower than expected inflation.

With a contribution of 0.5 pp, the food and non-alcoholic beverages division was no longer the main contributor to the YoY inflation in February, as it was replaced after 14 months by housing, in terms of weight the most significant division, whose contribution was 0.6 pp. The contribution of administrative measures to YoY inflation was only 0.2 pp, which was due to a contribution of regulated prices, especially of electricity.

The aforementioned error in the last forecast is one of the reasons for a decrease in the forecast for average inflation rate in 2018. Furthermore, this adjustment results from slightly altered assumptions. In comparison with the January forecast, we assume a stronger exchange rate of the koruna against the euro and even more significantly against the US dollar. The expected dollar crude oil price was also decreased slightly.

Administrative measures should only play a negligible role in the **2018** inflation. Among regulated prices, an increase in the price of electricity that occurred in January (contribution of 0.1 pp) and the pending introduction of discounts in transportation could be mentioned. As regards tax changes, consumer prices will reflect in particular a further increase in the excise taxes on tobacco products (a contribution of up to 0.1 pp). We expect the contribution of administrative measures to the YoY increase in consumer prices in December 2018 to reach 0.1 pp (*versus* 0.3 pp).

The YoY inflation should probably hover slightly above the CNB's 2% inflation target in the second and third quarters, and slow down in the fourth quarter. An important anti-inflationary factor will be the anticipated significant appreciation of the Czech koruna against the euro by 4.7%. On the other hand, one should expect an intensive pro-inflationary effect of the continued strong growth in unit labour costs and the growth in domestic demand against the backdrop of a positive output gap. Higher (in YoY terms) crude oil price will also play a role.

**In 2018**, the **average inflation rate** should reach 2.1% (*versus* 2.6%), with a YoY increase in consumer prices of 2.0% (*versus* 2.4%) in December.

**In 2019**, the pro-inflationary effect of several factors should be mitigated. The increase in unit labour costs and in domestic demand should slow down, and the

crude oil price should even decline. The output gap, however, will probably remain in clearly positive values. Further appreciation of the Czech koruna should have an anti-inflationary effect, although less marked than in 2018. Administrative measures should not play a significant role even in the next year's inflation.

In accordance with the above, we expect the **average inflation rate** to slow down to 1.9% (*versus* 2.1%) **in 2019** and the December YoY consumer prices growth to slow down to 1.8% (*versus* 1.9%). A possible shift of certain services and goods to the second reduced VAT rate is an anti-inflationary risk for 2019.

### 3.2.2 Deflators

In the fourth quarter of 2017, the GDP deflator increased by 2.4% (*versus* 1.9%), with the gross domestic expenditure deflator rising by 2.5% (*versus* 2.3%) and the terms of trade improving by 0.3% (*versus* 0.0%). As regards the gross domestic expenditure deflator, a slightly faster than expected growth in the deflators of household and the general government sector consumption and slower than expected growth in the gross capital formation deflator partially offset each other. In the case of the terms of trade, there was a deeper than expected decline in export prices; however, a deviation was also recorded on the import price side.

For the entire 2017, the GDP deflator thus increased by 1.4% (*versus* 1.3%). In 2018, its growth should slightly accelerate to 1.5% (*versus* 1.8%), with the effects of a slower growth in the gross domestic expenditure deflator and a more favourable terms of trade development than in 2017 acting against each other. In 2019, the growth in GDP deflator could accelerate further to 1.8% (*versus* 1.7%). The situation is clearly shown in Graph 3.2.6.

The expected development of the export and import prices will be influenced mainly by the anticipated appreciation of the koruna exchange rate and the crude oil price dynamics. As a result, the terms of trade could improve slightly by 0.1% (*versus* a deterioration of 0.2%) in 2018, and they could stagnate (*unchanged*) in 2019.

The growth in the gross domestic expenditure deflator could slow down from 2.4% (*versus* 2.3%) in 2017 to 1.8% (*versus* 2.2%) in 2018, with a reduced growth in all its components (see Graph 3.2.4). In 2019, the gross domestic expenditure deflator dynamics could increase marginally to 1.9% (*versus* 1.8%) as a result of an acceleration of the salary growth in the general government sector (especially in regional education).

**Table 3.2.1: Prices – yearly**

		2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
								Forecast	Forecast	Outlook	Outlook
<b>Consumer Price Index</b>											
<b>Average of a year</b>	<i>average 2005=100</i>	121.0	122.7	123.2	123.6	124.4	127.4	130.0	132.6	135.0	137.4
	<i>growth in %</i>	<b>3.3</b>	<b>1.4</b>	<b>0.4</b>	<b>0.3</b>	<b>0.7</b>	<b>2.5</b>	<b>2.1</b>	<b>1.9</b>	<b>1.8</b>	<b>1.8</b>
<b>December</b>	<i>average 2005=100</i>	121.1	122.8	122.9	123.0	125.4	128.3	130.9	133.3	135.7	138.1
	<i>growth in %</i>	<b>2.4</b>	<b>1.4</b>	<b>0.1</b>	<b>0.1</b>	<b>2.0</b>	<b>2.4</b>	<b>2.0</b>	<b>1.8</b>	<b>1.8</b>	<b>1.8</b>
<b>Of which the contribution of:</b>											
Administrative measures <sup>1)</sup>	<i>percentage points</i>	<b>2.2</b>	<b>1.0</b>	<b>-0.2</b>	<b>0.1</b>	<b>0.0</b>	<b>0.1</b>	<b>0.1</b>	<b>0.3</b>	<b>0.3</b>	<b>0.3</b>
Market increase	<i>percentage points</i>	<b>0.2</b>	<b>0.4</b>	<b>0.3</b>	<b>0.0</b>	<b>2.0</b>	<b>2.3</b>	<b>1.9</b>	<b>1.6</b>	<b>1.5</b>	<b>1.5</b>
<b>Harmonized index of consumer prices</b>	<i>average 2005=100</i>	120.3	121.9	122.4	122.8	123.6	126.6	129.0	131.5	133.8	136.1
	<i>growth in %</i>	<b>3.5</b>	<b>1.4</b>	<b>0.4</b>	<b>0.3</b>	<b>0.6</b>	<b>2.4</b>	<b>1.9</b>	<b>1.9</b>	<b>1.8</b>	<b>1.7</b>
<b>Offering prices of flats</b>											
<b>Czech Republic</b>	<i>average 2010=100</i>	96.1	97.2	100.7	106.9	117.6	130.7	.	.	.	.
	<i>growth in %</i>	<b>1.1</b>	<b>1.1</b>	<b>3.6</b>	<b>6.2</b>	<b>10.0</b>	<b>11.1</b>	.	.	.	.
<b>Czech Republic excluding Prague</b>	<i>average 2010=100</i>	92.5	91.3	93.0	97.7	107.1	112.1	.	.	.	.
	<i>growth in %</i>	<b>-4.2</b>	<b>-1.3</b>	<b>1.9</b>	<b>5.1</b>	<b>9.6</b>	<b>4.7</b>	.	.	.	.
<b>Prague</b>	<i>average 2010=100</i>	99.6	103.1	108.5	116.1	128.2	149.2	.	.	.	.
	<i>growth in %</i>	<b>6.4</b>	<b>3.5</b>	<b>5.2</b>	<b>7.0</b>	<b>10.4</b>	<b>16.4</b>	.	.	.	.
<b>Deflators</b>											
<b>GDP</b>	<i>average 2010=100</i>	101.5	102.9	105.5	106.7	108.0	109.6	111.3	113.3	115.2	117.4
	<i>growth in %</i>	<b>1.5</b>	<b>1.4</b>	<b>2.5</b>	<b>1.2</b>	<b>1.2</b>	<b>1.4</b>	<b>1.5</b>	<b>1.8</b>	<b>1.7</b>	<b>1.9</b>
<b>Domestic final use</b>	<i>average 2010=100</i>	102.9	103.5	104.6	105.7	106.4	109.0	111.0	113.1	115.0	117.1
	<i>growth in %</i>	<b>1.8</b>	<b>0.5</b>	<b>1.1</b>	<b>1.0</b>	<b>0.7</b>	<b>2.4</b>	<b>1.8</b>	<b>1.9</b>	<b>1.7</b>	<b>1.8</b>
<b>Consumption of households</b>	<i>average 2010=100</i>	104.0	104.9	105.5	105.6	106.1	108.7	111.1	113.3	115.3	117.4
	<i>growth in %</i>	<b>2.2</b>	<b>0.8</b>	<b>0.6</b>	<b>0.1</b>	<b>0.5</b>	<b>2.5</b>	<b>2.2</b>	<b>2.0</b>	<b>1.8</b>	<b>1.8</b>
<b>Consumption of government</b>	<i>average 2010=100</i>	102.7	102.8	104.6	106.7	108.7	113.1	116.5	120.9	123.8	126.9
	<i>growth in %</i>	<b>0.9</b>	<b>0.2</b>	<b>1.7</b>	<b>2.0</b>	<b>1.8</b>	<b>4.0</b>	<b>3.0</b>	<b>3.8</b>	<b>2.4</b>	<b>2.5</b>
<b>Fixed capital formation</b>	<i>average 2010=100</i>	100.9	101.1	102.7	104.5	104.8	106.2	106.7	107.4	108.4	109.9
	<i>growth in %</i>	<b>1.7</b>	<b>0.1</b>	<b>1.6</b>	<b>1.8</b>	<b>0.3</b>	<b>1.3</b>	<b>0.5</b>	<b>0.6</b>	<b>0.9</b>	<b>1.4</b>
<b>Exports of goods and services</b>	<i>average 2010=100</i>	103.8	105.6	109.8	108.4	105.7	104.7	101.4	101.2	101.6	102.2
	<i>growth in %</i>	<b>3.1</b>	<b>1.7</b>	<b>4.0</b>	<b>-1.3</b>	<b>-2.5</b>	<b>-0.9</b>	<b>-3.2</b>	<b>-0.2</b>	<b>0.4</b>	<b>0.5</b>
<b>Imports of goods and services</b>	<i>average 2010=100</i>	106.1	106.6	109.2	107.4	103.6	103.7	100.3	100.1	100.4	100.7
	<i>growth in %</i>	<b>3.7</b>	<b>0.5</b>	<b>2.5</b>	<b>-1.7</b>	<b>-3.5</b>	<b>0.1</b>	<b>-3.3</b>	<b>-0.2</b>	<b>0.3</b>	<b>0.3</b>
<b>Terms of trade</b>	<i>average 2010=100</i>	97.9	99.0	100.5	100.9	102.0	101.0	101.1	101.1	101.2	101.4
	<i>growth in %</i>	<b>-0.6</b>	<b>1.2</b>	<b>1.5</b>	<b>0.4</b>	<b>1.1</b>	<b>-1.0</b>	<b>0.1</b>	<b>0.0</b>	<b>0.1</b>	<b>0.2</b>

<sup>1)</sup> The contribution of increase in regulated prices and in indirect taxes to increase of December YoY consumer price inflation.

Source: CZSO, Eurostat. Calculations of the MoF.

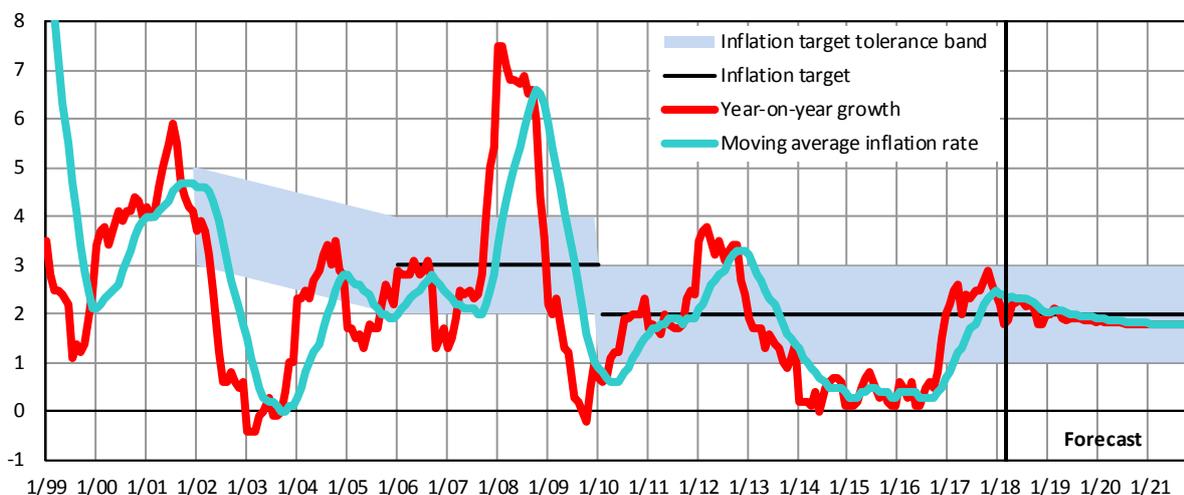
**Table 3.2.2: Prices – quarterly**

		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
						Estimate	Forecast	Forecast	Forecast
<b>Consumer Price Index</b>	<i>average 2005=100</i>	126.7	127.1	127.6	128.3	129.2	130.0	130.4	130.7
	<i>growth in %</i>	2.4	2.2	2.5	2.6	2.0	2.3	2.2	1.8
<b>Of which the contribution of:</b>									
Administrative measures <sup>1)</sup>	<i>percentage points</i>	-0.2	-0.2	-0.1	-0.1	0.2	0.2	0.1	0.1
Market increase	<i>percentage points</i>	2.6	2.4	2.6	2.7	1.7	2.0	2.1	1.7
<b>Harmonized index of consumer prices</b>	<i>average 2005=100</i>	125.9	126.3	126.7	127.3	128.2	129.0	129.4	129.6
	<i>growth in %</i>	2.5	2.3	2.4	2.5	1.8	2.1	2.1	1.8
<b>Offering prices of flats</b>									
<b>Czech Republic</b>	<i>average 2010=100</i>	124.2	127.6	133.7	137.1	.	.	.	.
	<i>growth in %</i>	9.5	9.5	12.5	12.5	.	.	.	.
<b>Czech Republic excluding Prague</b>	<i>average 2010=100</i>	108.3	109.9	114.6	115.4	.	.	.	.
	<i>growth in %</i>	4.6	3.6	5.7	4.7	.	.	.	.
<b>Prague</b>	<i>average 2010=100</i>	140.0	145.3	152.8	158.8	.	.	.	.
	<i>growth in %</i>	13.6	14.6	18.3	18.8	.	.	.	.
<b>Deflators</b>									
<b>GDP</b>	<i>average 2010=100</i>	108.1	108.8	109.8	111.4	109.6	110.4	111.6	113.3
	<i>growth in %</i>	0.6	1.0	1.6	2.4	1.4	1.5	1.6	1.6
<b>Domestic final use</b>	<i>average 2010=100</i>	107.7	108.5	109.0	110.7	109.7	110.5	111.0	112.6
	<i>growth in %</i>	2.2	2.5	2.5	2.5	1.8	1.9	1.9	1.6
<b>Consumption of households</b>	<i>average 2010=100</i>	107.8	108.1	109.0	109.9	110.1	110.7	111.5	112.0
	<i>growth in %</i>	2.4	2.2	2.4	2.8	2.1	2.4	2.3	1.9
<b>Consumption of government</b>	<i>average 2010=100</i>	108.4	111.4	112.3	119.1	112.0	115.1	115.9	122.0
	<i>growth in %</i>	3.1	3.8	4.0	5.0	3.3	3.4	3.2	2.4
<b>Fixed capital formation</b>	<i>average 2010=100</i>	106.5	106.4	106.2	105.8	106.9	106.7	106.7	106.6
	<i>growth in %</i>	1.6	1.7	1.4	0.8	0.3	0.3	0.5	0.7
<b>Exports of goods and services</b>	<i>average 2010=100</i>	107.0	105.6	103.6	102.6	101.7	101.3	101.3	101.2
	<i>growth in %</i>	1.4	0.3	-1.9	-3.3	-4.9	-4.1	-2.3	-1.4
<b>Imports of goods and services</b>	<i>average 2010=100</i>	106.5	105.0	102.3	101.3	101.1	100.6	99.8	99.7
	<i>growth in %</i>	3.5	2.0	-1.1	-3.6	-5.1	-4.2	-2.4	-1.6
<b>Terms of trade</b>	<i>average 2010=100</i>	100.5	100.6	101.3	101.3	100.7	100.7	101.5	101.5
	<i>growth in %</i>	-2.0	-1.7	-0.8	0.3	0.2	0.1	0.1	0.2

<sup>1)</sup> The contribution of increase in regulated prices and in indirect taxes to increase of December YoY consumer price inflation.  
Source: CZSO, Eurostat. Calculations of the MoF.

**Graph 3.2.1: Consumer Prices**

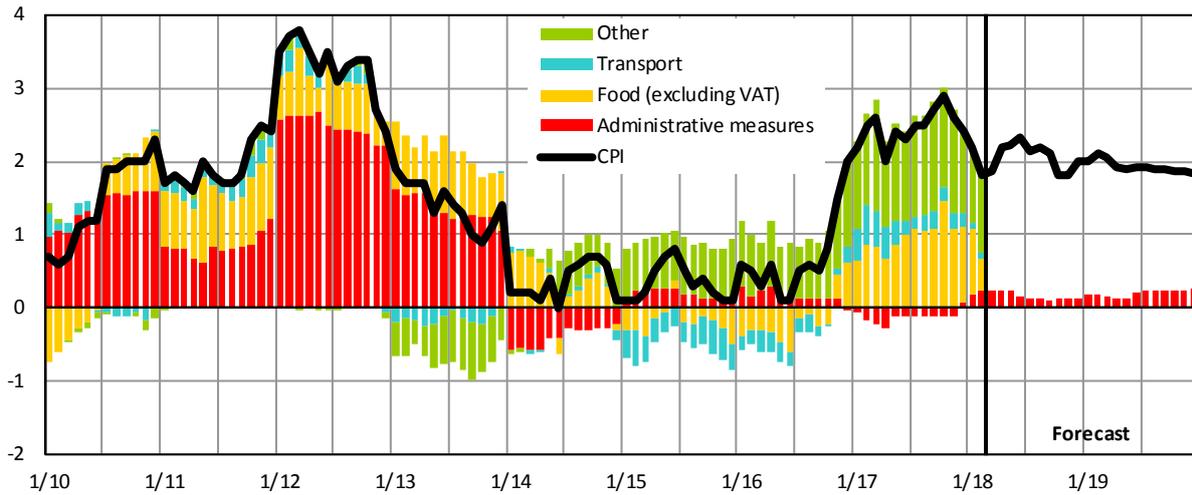
YoY growth rate, in %



Note: For the years 2002–2005 the highlighted area represents target band for headline inflation, whereas from 2006 on it is the tolerance band of the CNB's point target for headline inflation.  
Source: CNB, CZSO. Calculations of the MoF.

### Graph 3.2.2: Consumer Prices in Main Divisions

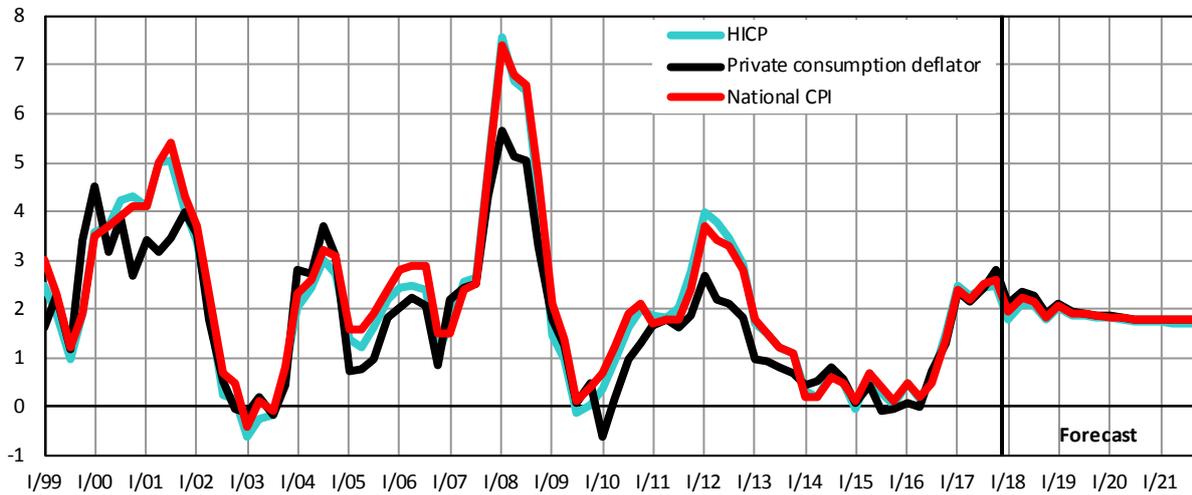
YoY growth of consumer price index, contributions in percentage points, Transport excluding administrative measures and excises



Source: CZSO. Calculations of the MoF.

### Graph 3.2.3: Indicators of Consumer Prices

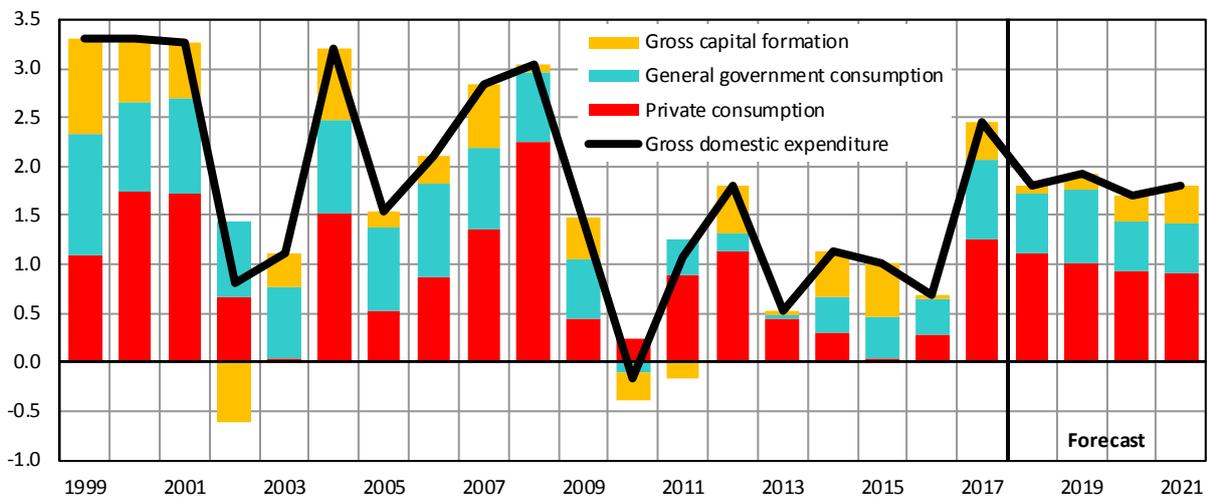
YoY growth rate, in %



Source: CZSO, Eurostat. Calculations of the MoF.

### Graph 3.2.4: Gross Domestic Expenditure Deflator

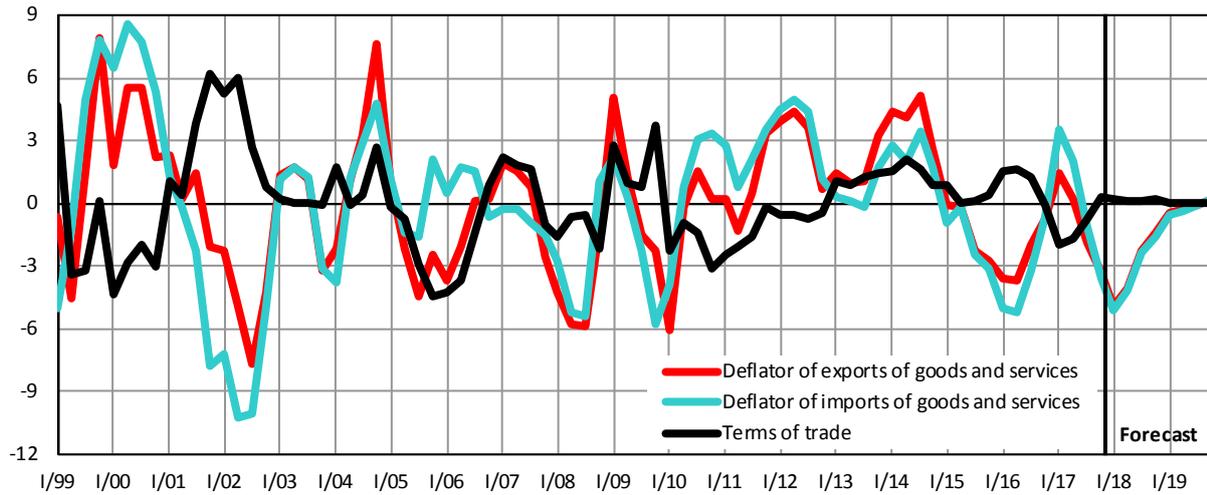
YoY growth rate in %, contributions of growth of deflators of individual components of gross domestic expenditure in percentage points



Source: CZSO. Calculations of the MoF.

### Graph 3.2.5: Terms of Trade

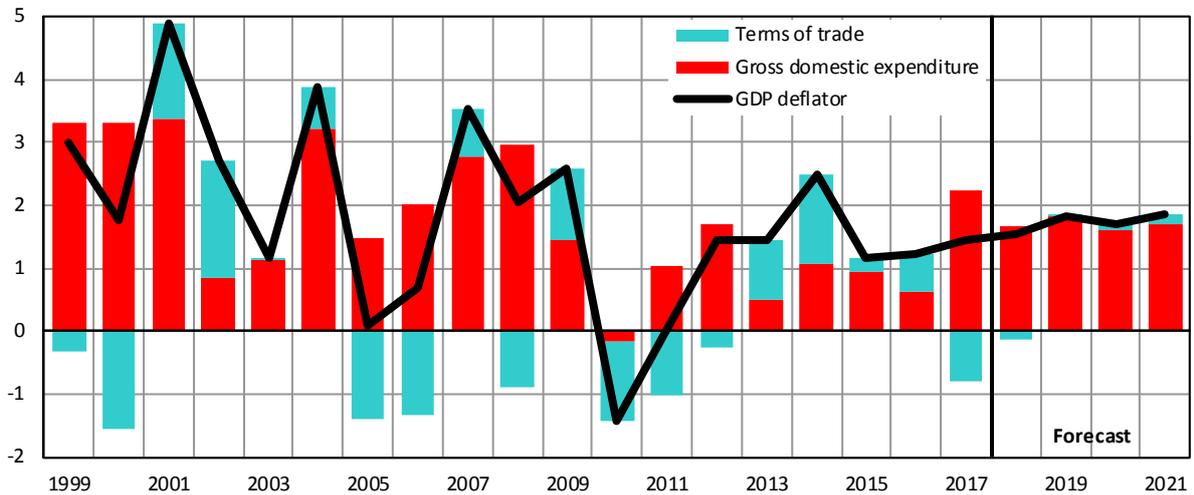
YoY growth rate, in %



Source: CZSO. Calculations of the MoF.

### Graph 3.2.6: GDP deflator

YoY change in %, contributions of growth of gross domestic expenditure deflator and change in terms of trade in percentage points



Source: CZSO. Calculations of the MoF.

### 3.3 Labour Market

The labour market is showing symptoms of overheating. Growth in employment continued, according to all available statistics. Registered unemployment declines further, whereas the internationally comparable unemployment rate according to the LFS has probably hit the bottom. The number of vacancies is almost 250 thousand, exceeding the previous highs from 2008 by more than a half. This development is fully correlated with a strong growth in wages and salaries.

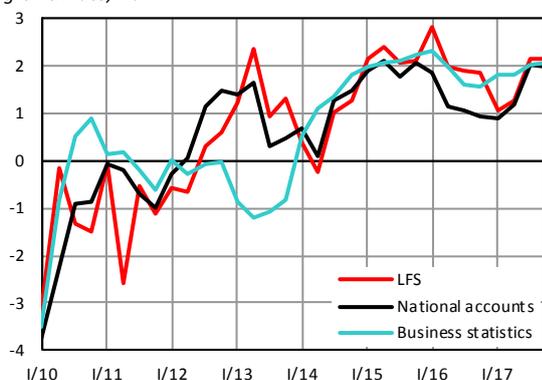
#### 3.3.1 Employment

Employment (LFS) grew by 1.5% YoY (*versus 1.3%*) in the fourth quarter of 2017. The number of employees increased by 2.1% (*versus 1.2%*), the number of entrepreneurs, however, decreased by 1.8%. That was due to a decline in the number of entrepreneurs without employees by 1.6% as well as by a sharp decrease in the category of helping family members (formally in the category of entrepreneurs). Growth in the number of entrepreneurs with employees slowed down to 0.2%.

From the sectoral perspective, the employment growth (business statistics) was in absolute terms primarily driven by manufacturing; major increases were also recorded in energy industry, information and communication activities, or in accommodation and food service activities. A strong decline continued in mining and quarrying, and was also recorded in construction and administrative and support service activities.

**Graph 3.3.1: Employees in Different Statistics**

YoY growth rate, in%



Source: CZSO.

Shortage of workers is evident virtually in all sectors of the economy and is already a major obstacle to economic growth driven by the use of labour force.

The possibility of further employment growth through the use of the unemployed is, to a large extent, exhausted. A natural response is to attract workers from among the economically inactive persons. Another possible solution to the shortage of employees is recruitment of foreign workers, which, however, often faces administrative barriers. In the longer term, room is thus being created for the development of automation and robotiza-

tion and greater orientation of the economy to less labour-intensive sectors with higher value added.

Thanks to the higher growth in the fourth quarter of 2017, we are slightly increasing the forecast for employment growth in 2018 to 0.7% (*versus 0.6%*). Due to the lack of labour force described above, we expect the growth to slow down to 0.2% (*unchanged*) in 2019.

#### 3.3.2 Unemployment

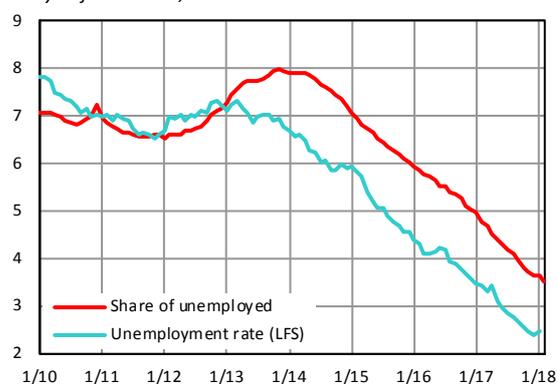
The drop in the **unemployment rate** (LFS) to new record lows continued also in the fourth quarter of 2017, when this indicator reached 2.4% (*versus 2.5%*). Seasonally adjusted unemployment rate in the 15–64 age group hovered at this level also in January 2018. The number of unemployed persons declined by 63 thousand YoY in the fourth quarter. Intensity of the decline is no longer sustainable – the unemployment rate is likely to have almost reached its bottom.

In 2017 as a whole the unemployment rate averaged 2.9% (*in line with the estimate*). For 2018, we forecast a decline to 2.4%, and for 2019 a slight decrease to 2.3% (*unchanged for both years*).

The YoY fall in the **share of unemployed persons** (Ministry of Labour and Social Affairs) has been 1.4 pp since September 2017; in absolute terms, the number of registered unemployed has been decreasing by approximately 100 thousand. As regards registered unemployment, there is greater room for further decline than in the case of the LFS due to the fact that a part of applicants are engaged in a so-called non-conflicting part-time employment, and they are thus probably able to exit registration and take on a full-time job. For the coming period, we expect the share of unemployed persons to decrease to 3.3% in 2018 and further to 2.8% in 2019 (*unchanged for both years*).

**Graph 3.3.2: Indicators of Unemployment**

seasonally adjusted data, in%



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.

Source: CZSO, Ministry of Labour and Social Affairs. Calculations of the MoF.

### 3.3.3 Participation

The economic activity rate (15–64 year-olds) grew by 0.5 pp YoY to 76.2% in the fourth quarter of 2017 (*in line with the estimate*). The very high number of job vacancies and increasing earnings motivate previously economically inactive individuals to engage in the labour process. We suppose there is still room for a further growth in the participation rate, with demographic aspects in the form of an increasing weight of cohorts with naturally high economic activity rate (especially of those aged 40–49 years) and gradual increases in the statutory as well as actual retirement age playing the main role.

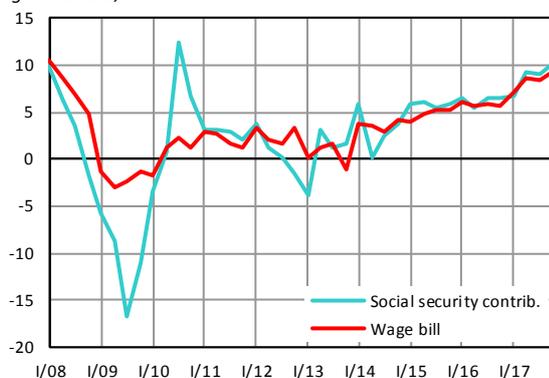
For 2018, we thus expect the participation rate to grow by 0.6 pp to 76.5% (*unchanged*), and for 2019 we expect another increase to 77.0% (*unchanged*).

### 3.3.4 Wages

The wage bill growth (national accounts, domestic concept) accelerated sharply and reached 9.1% in the fourth quarter of 2017 (*versus 8.3%*). Extremely high growth was recorded in public administration, defence, education and health care (11.7%). The dynamics of earnings were in large part driven by manufacturing, where wages rose by 9.0%. The slowest growth rate was recorded in construction (5.1%), but the dynamics accelerated significantly compared to the previous quarter. In 2017 as a whole the wage bill at the domestic economy level increased by 8.3% (*versus 7.9%*).

**Graph 3.3.3: Collection of Social Security Contributions and the Wage Bill**

YoY growth rate, in%



Note: Time series of the collection of social security contributions is influenced, among other factors, by a legislative change in 2009 and a pay-out of exceptional bonuses at the end of 2012.

Source: CZSO, Ministry of Finance.

The continued wage dynamics are reflected in the development of social security contributions from the state budget cash collection, which grew by 9.8% in the first three months of 2018. We estimate that the growth of

the wage bill reached 8.3% (*versus 8.0%*) in the first quarter of 2018.

This year we expect persistent frictions in the labour market associated with the shortage of labour force in the economy. Moreover, wages and salaries are supported by an increase in the minimum and guaranteed wages (by 11.1%) and an increase in salary scales in health care (10%), which is effective from the beginning of 2018. Major part of the year will also be affected by the increase in salary scales in the general government sector from the second half of 2017. The wage bill could rise by 7.7% (*unchanged*) in 2018.

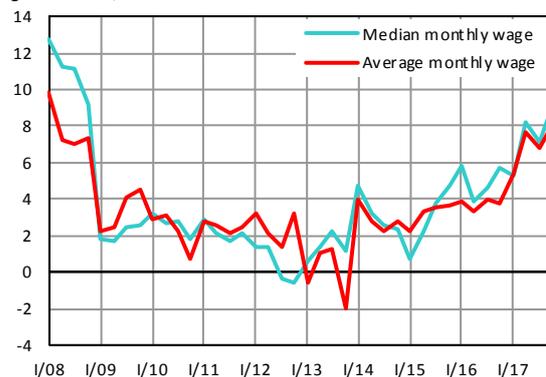
For 2019, we anticipate a weakening of the dynamics of demand for labour force due to a slowdown in economic growth. In addition, it is not possible to rule out acceleration of the process of replacing certain jobs with capital due to a significant increase in the price of labour force and the unavailability of suitably qualified workers. Any changes in minimum and guaranteed wages have not yet been decided. The growth in the wage bill could therefore slow down to 6.5% (*versus 4.9%*) in 2019.

The **average wage** (business statistics, full-time equivalent) increased by 8.0% (*versus 8.1%*) in the fourth quarter of 2017. Thanks to a strong growth in medium-earning professions, the growth rate of the wage median was 8.9% over the same period. The average nominal wage increased by 7.0% (*versus 6.9%*) and the average real wage by 4.5% (*versus 4.4%*) in 2017.

Due to a very tight labour market situation, the average nominal wage could increase by 7.3% (*versus 7.1%*) in 2018. In the coming years, we expect the above-mentioned slowdown in demand for labour. In 2019, the YoY growth rate of average wage could slow down to 6.3% (*versus 4.7%*).

**Graph 3.3.4: Nominal Monthly Wage**

YoY growth rate, in%



Source: CZSO.

**Table 3.3.1: Labour Market – yearly**

		2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
								Forecast	Forecast	Outlook	Outlook
<b>Labour Force Survey</b>											
<b>Employment</b>	<i>av. in thous.persons</i>	<b>4 890</b>	<b>4 937</b>	<b>4 974</b>	<b>5 042</b>	<b>5 139</b>	<b>5 222</b>	<b>5 256</b>	<b>5 264</b>	<b>5 272</b>	<b>5 277</b>
	<i>growth in %</i>	0.4	1.0	0.8	1.4	1.9	1.6	0.7	0.2	0.2	0.1
Employees	<i>av. in thous.persons</i>	<b>3 997</b>	<b>4 055</b>	<b>4 079</b>	<b>4 168</b>	<b>4 257</b>	<b>4 327</b>	<b>4 357</b>	<b>4 365</b>	<b>4 372</b>	<b>4 378</b>
	<i>growth in %</i>	-0.1	1.5	0.6	2.2	2.1	1.7	0.7	0.2	0.2	0.1
Entrepreneurs and self-employed	<i>av. in thous.persons</i>	<b>893</b>	<b>882</b>	<b>895</b>	<b>874</b>	<b>882</b>	<b>894</b>	<b>899</b>	<b>899</b>	<b>900</b>	<b>900</b>
	<i>growth in %</i>	2.4	-1.3	1.5	-2.3	0.9	1.4	0.5	0.1	0.1	0.0
<b>Unemployment</b>	<i>av. in thous.persons</i>	<b>367</b>	<b>369</b>	<b>324</b>	<b>268</b>	<b>211</b>	<b>156</b>	<b>131</b>	<b>127</b>	<b>125</b>	<b>124</b>
<b>Unemployment rate</b>	<i>average in %</i>	<b>7.0</b>	<b>7.0</b>	<b>6.1</b>	<b>5.1</b>	<b>4.0</b>	<b>2.9</b>	<b>2.4</b>	<b>2.3</b>	<b>2.3</b>	<b>2.3</b>
<b>Long-term unemployment <sup>1)</sup></b>	<i>av. in thous.persons</i>	<b>161</b>	<b>163</b>	<b>141</b>	<b>127</b>	<b>89</b>	.	.	.	.	.
<b>Labour force</b>	<i>av. in thous.persons</i>	<b>5 257</b>	<b>5 306</b>	<b>5 298</b>	<b>5 310</b>	<b>5 350</b>	<b>5 377</b>	<b>5 387</b>	<b>5 391</b>	<b>5 397</b>	<b>5 402</b>
	<i>growth in %</i>	0.7	0.9	-0.2	0.2	0.8	0.5	0.2	0.1	0.1	0.1
<b>Population aged 15–64</b>	<i>av. in thous.persons</i>	<b>7 229</b>	<b>7 154</b>	<b>7 081</b>	<b>7 026</b>	<b>6 968</b>	<b>6 917</b>	<b>6 870</b>	<b>6 827</b>	<b>6 789</b>	<b>6 760</b>
	<i>growth in %</i>	-0.9	-1.0	-1.0	-0.8	-0.8	-0.7	-0.7	-0.6	-0.5	-0.4
<b>Employment/Pop. 15–64</b>	<i>average in %</i>	<b>67.6</b>	<b>69.0</b>	<b>70.2</b>	<b>71.8</b>	<b>73.7</b>	<b>75.5</b>	<b>76.5</b>	<b>77.1</b>	<b>77.7</b>	<b>78.1</b>
<b>Employment rate 15–64 <sup>2)</sup></b>	<i>average in %</i>	<b>66.5</b>	<b>67.7</b>	<b>69.0</b>	<b>70.2</b>	<b>72.0</b>	<b>73.6</b>	<b>74.6</b>	<b>75.2</b>	<b>75.7</b>	<b>76.1</b>
<b>Labour force/Pop. 15–64</b>	<i>average in %</i>	<b>72.7</b>	<b>74.2</b>	<b>74.8</b>	<b>75.6</b>	<b>76.8</b>	<b>77.7</b>	<b>78.4</b>	<b>79.0</b>	<b>79.5</b>	<b>79.9</b>
<b>Participation rate 15–64 <sup>3)</sup></b>	<i>average in %</i>	<b>71.6</b>	<b>72.9</b>	<b>73.5</b>	<b>74.0</b>	<b>75.0</b>	<b>75.9</b>	<b>76.5</b>	<b>77.0</b>	<b>77.5</b>	<b>77.9</b>
<b>Registered unemployment</b>											
<b>Unemployment</b>	<i>av. in thous.persons</i>	<b>504</b>	<b>564</b>	<b>561</b>	<b>479</b>	<b>406</b>	<b>318</b>	<b>238</b>	<b>202</b>	<b>186</b>	<b>185</b>
<b>Share of unemployed <sup>4)</sup></b>	<i>average in %</i>	<b>6.8</b>	<b>7.7</b>	<b>7.7</b>	<b>6.6</b>	<b>5.6</b>	<b>4.3</b>	<b>3.4</b>	<b>3.0</b>	<b>2.8</b>	<b>2.7</b>
<b>Wages and salaries</b>											
<b>Average monthly wage <sup>5)</sup></b>											
Nominal	CZK	25 067	25 035	25 768	26 591	27 575	29 504	31 600	33 600	35 400	37 300
	<i>growth in %</i>	<b>2.5</b>	<b>-0.1</b>	<b>2.9</b>	<b>3.2</b>	<b>3.7</b>	<b>7.0</b>	<b>7.3</b>	<b>6.3</b>	<b>5.3</b>	<b>5.3</b>
Real	CZK 2005	20 717	20 403	20 916	21 514	22 166	23 159	24 300	25 400	26 300	27 200
	<i>growth in %</i>	<b>-0.8</b>	<b>-1.5</b>	<b>2.5</b>	<b>2.9</b>	<b>3.0</b>	<b>4.5</b>	<b>5.1</b>	<b>4.3</b>	<b>3.4</b>	<b>3.5</b>
<b>Median monthly wage</b>	CZK	20 828	21 110	21 786	22 414	23 531	25 283	.	.	.	.
	<i>growth in %</i>	<b>0.4</b>	<b>1.4</b>	<b>3.2</b>	<b>2.9</b>	<b>5.0</b>	<b>7.4</b>	.	.	.	.
<b>Wage bill</b>	<i>growth in %</i>	<b>2.6</b>	<b>0.5</b>	<b>3.6</b>	<b>4.8</b>	<b>5.8</b>	<b>8.3</b>	<b>7.7</b>	<b>6.5</b>	<b>5.5</b>	<b>5.4</b>
<b>Labour productivity</b>	<i>growth in %</i>	<b>-1.2</b>	<b>-0.8</b>	<b>2.2</b>	<b>3.8</b>	<b>1.3</b>	<b>2.8</b>	<b>3.0</b>	<b>3.2</b>	<b>2.5</b>	<b>2.3</b>
<b>Unit labour costs <sup>6)</sup></b>	<i>growth in %</i>	<b>3.0</b>	<b>0.5</b>	<b>0.4</b>	<b>-0.8</b>	<b>3.3</b>	<b>3.8</b>	<b>3.9</b>	<b>3.1</b>	<b>2.8</b>	<b>2.9</b>
<b>Compens. of employees / GDP</b>	%	<b>41.0</b>	<b>40.9</b>	<b>40.2</b>	<b>39.6</b>	<b>40.4</b>	<b>41.3</b>	<b>42.3</b>	<b>42.8</b>	<b>43.3</b>	<b>43.8</b>

<sup>1)</sup> Persons in unemployment for longer than 12 months.

<sup>2)</sup> The indicator does not include employment over 64 years.

<sup>3)</sup> The indicator does not include labour force over 64 years.

<sup>4)</sup> Share of available job seekers aged 15 to 64 years in the population of the same age.

<sup>5)</sup> Derived from full-time-equivalent employers in the entire economy.

<sup>6)</sup> Ratio of nominal compensation per employee to real productivity of labour.

Source: CZSO, Ministry of Labour and Social Affairs. Calculations of the MoF.

**Table 3.3.2: Labour Market – quarterly**

		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
						Estimate	Forecast	Forecast	Forecast
<b>Labour Force Survey</b>									
<b>Employment</b>	<i>av. in thous. persons</i>	<b>5 169</b>	<b>5 197</b>	<b>5 257</b>	<b>5 263</b>	<b>5 229</b>	<b>5 257</b>	<b>5 267</b>	<b>5 271</b>
	<i>YoY growth in %</i>	1.6	1.3	2.0	1.5	1.1	1.2	0.2	0.1
	<i>QoQ growth in %</i>	0.3	0.0	1.0	0.1	0.0	0.0	0.0	0.0
Employees	<i>av. in thous. persons</i>	<b>4 276</b>	<b>4 298</b>	<b>4 360</b>	<b>4 375</b>	<b>4 328</b>	<b>4 349</b>	<b>4 369</b>	<b>4 382</b>
	<i>growth in %</i>	1.1	1.3	2.2	2.1	1.2	1.2	0.2	0.2
Entrepreneurs and self-employed	<i>av. in thous. persons</i>	<b>893</b>	<b>899</b>	<b>897</b>	<b>888</b>	<b>901</b>	<b>908</b>	<b>898</b>	<b>888</b>
	<i>growth in %</i>	4.4	1.6	1.5	-1.8	0.9	1.1	0.1	0.1
<b>Unemployment</b>	<i>av. in thous. persons</i>	<b>185</b>	<b>159</b>	<b>150</b>	<b>129</b>	<b>136</b>	<b>128</b>	<b>132</b>	<b>128</b>
<b>Unemployment rate</b>	<i>average in %</i>	<b>3.4</b>	<b>3.0</b>	<b>2.8</b>	<b>2.4</b>	<b>2.5</b>	<b>2.4</b>	<b>2.4</b>	<b>2.4</b>
<b>Long-term unemployment<sup>1)</sup></b>	<i>av. in thous. persons</i>	<b>68</b>	<b>59</b>	<b>49</b>	.	.	.	.	.
<b>Labour force</b>	<i>av. in thous. persons</i>	<b>5 354</b>	<b>5 356</b>	<b>5 407</b>	<b>5 391</b>	<b>5 365</b>	<b>5 385</b>	<b>5 399</b>	<b>5 399</b>
	<i>growth in %</i>	0.7	0.3	0.8	0.2	0.2	0.5	-0.2	0.1
<b>Population aged 15–64</b>	<i>av. in thous. persons</i>	<b>6 936</b>	<b>6 921</b>	<b>6 911</b>	<b>6 900</b>	<b>6 888</b>	<b>6 876</b>	<b>6 864</b>	<b>6 852</b>
	<i>growth in %</i>	-0.8	-0.8	-0.7	-0.7	-0.7	-0.6	-0.7	-0.7
<b>Employment/Pop. 15–64</b>	<i>average in %</i>	<b>74.5</b>	<b>75.1</b>	<b>76.1</b>	<b>76.3</b>	<b>75.9</b>	<b>76.5</b>	<b>76.7</b>	<b>76.9</b>
	<i>increase over a year</i>	1.8	1.6	2.1	1.6	1.4	1.4	0.7	0.6
<b>Employment rate 15–64<sup>2)</sup></b>	<i>average in %</i>	<b>72.8</b>	<b>73.3</b>	<b>74.1</b>	<b>74.3</b>	<b>74.0</b>	<b>74.6</b>	<b>74.8</b>	<b>75.0</b>
	<i>increase over a year</i>	1.8	1.6	1.9	1.4	1.2	1.3	0.7	0.7
<b>Labour force/Pop. 15–64</b>	<i>average in %</i>	<b>77.2</b>	<b>77.4</b>	<b>78.2</b>	<b>78.1</b>	<b>77.9</b>	<b>78.3</b>	<b>78.7</b>	<b>78.8</b>
	<i>increase over a year</i>	1.1	0.9	1.2	0.7	0.7	0.9	0.4	0.6
<b>Participation rate 15–64<sup>3)</sup></b>	<i>average in %</i>	<b>75.5</b>	<b>75.6</b>	<b>76.3</b>	<b>76.2</b>	<b>76.0</b>	<b>76.4</b>	<b>76.7</b>	<b>76.9</b>
	<i>increase over a year</i>	1.1	0.8	1.0	0.5	0.5	0.8	0.4	0.7
<b>Registered unemployment</b>									
<b>Unemployment</b>	<i>av. in thous. persons</i>	<b>379.5</b>	<b>320.8</b>	<b>297.0</b>	<b>273.1</b>	<b>280</b>	<b>234</b>	<b>221</b>	<b>216</b>
<b>Share of unemployed<sup>4)</sup></b>	<i>average in %</i>	<b>5.1</b>	<b>4.3</b>	<b>4.0</b>	<b>3.6</b>	<b>3.8</b>	<b>3.4</b>	<b>3.2</b>	<b>3.1</b>
<b>Wages and salaries</b>									
<b>Average monthly wage<sup>5)</sup></b>									
Nominal	CZK	27 907	29 352	29 063	31 646	30 000	31 500	31 300	33 800
	<i>growth in %</i>	<b>5.4</b>	<b>7.6</b>	<b>6.8</b>	<b>8.0</b>	<b>7.6</b>	<b>7.2</b>	<b>7.6</b>	<b>6.8</b>
Real	CZK 2005	22 026	23 094	22 777	24 666	23 200	24 200	24 000	25 900
	<i>growth in %</i>	<b>2.9</b>	<b>5.3</b>	<b>4.2</b>	<b>5.2</b>	<b>5.6</b>	<b>4.9</b>	<b>5.3</b>	<b>4.9</b>
<b>Median monthly wage</b>	CZK	23 719	24 901	25 192	27 320	.	.	.	.
	<i>growth in %</i>	<b>5.3</b>	<b>8.2</b>	<b>7.2</b>	<b>8.9</b>	.	.	.	.
<b>Wage bill</b>	<i>growth in %</i>	<b>7.0</b>	<b>8.5</b>	<b>8.4</b>	<b>9.1</b>	<b>8.3</b>	<b>7.8</b>	<b>7.6</b>	<b>7.2</b>

<sup>1)</sup> Persons in unemployment for longer than 12 months.

<sup>2)</sup> The indicator does not include employment over 64 years.

<sup>3)</sup> The indicator does not include labour force over 64 years.

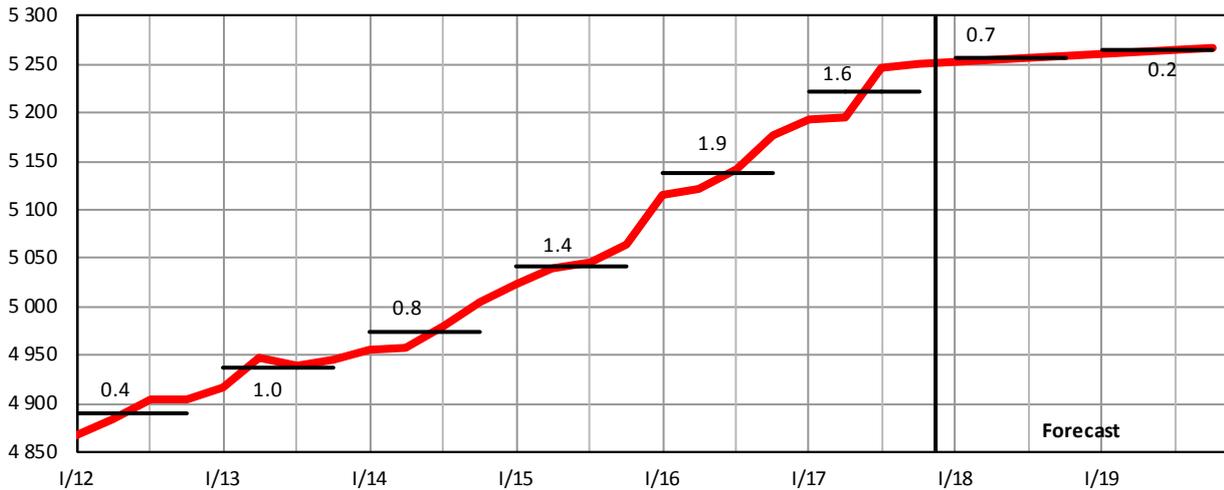
<sup>4)</sup> Share of available job seekers aged 15 to 64 years in the population of the same age.

<sup>5)</sup> Derived from full-time-equivalent employers in the entire economy.

Source: CZSO, Ministry of Labour and Social Affairs. Calculations of the MoF.

### Graph 3.3.5: Employment (LFS)

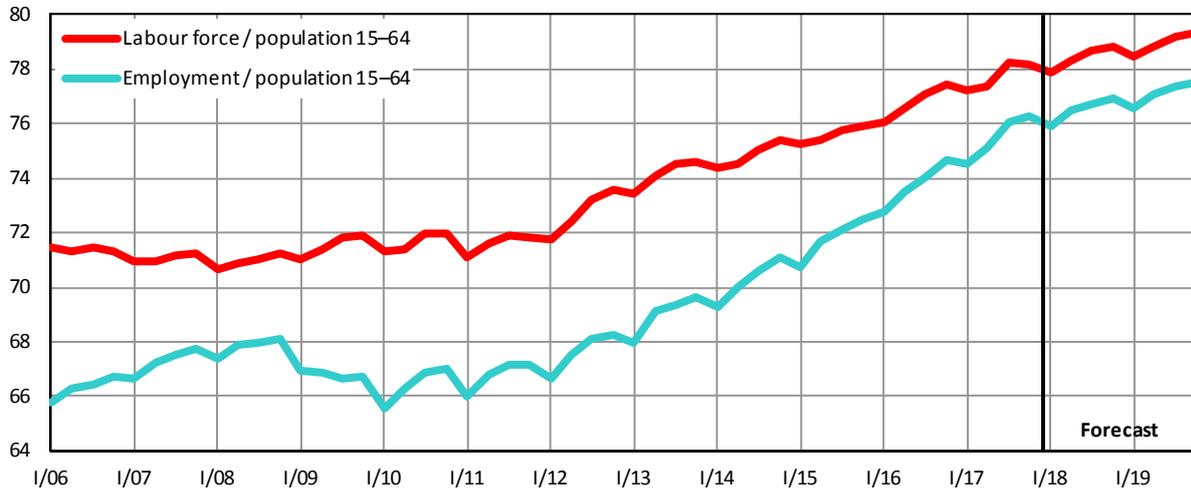
seasonally adjusted data, in thousands of persons, black lines with labels show the average level and growth rate in the given year



Source: CZSO. Calculations of the MoF.

### Graph 3.3.6: Ratio of Labour Force and Employment to Population Aged 15–64

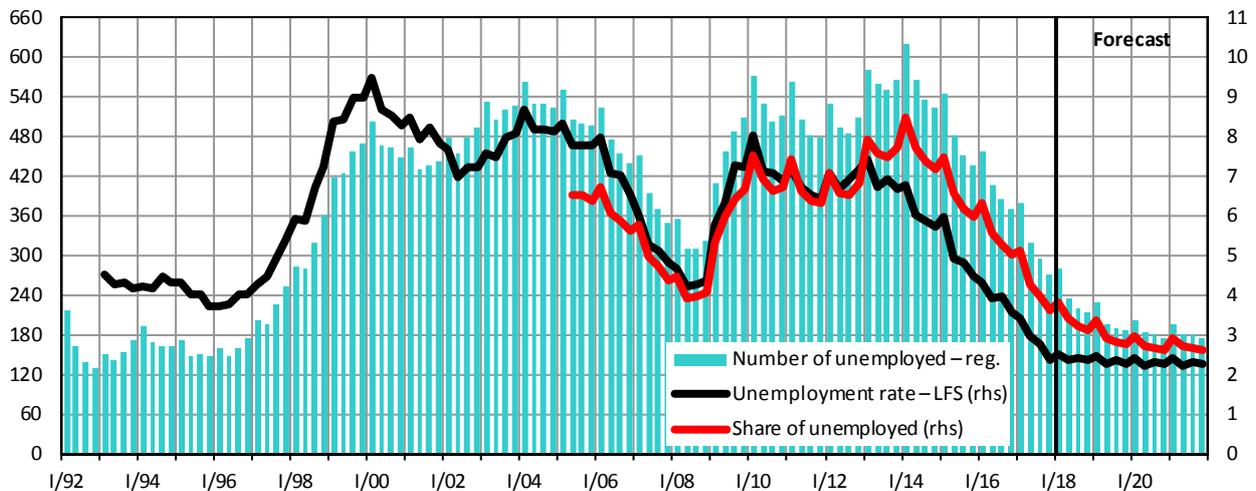
in %



Source: CZSO. Calculations of the MoF.

### Graph 3.3.7: Unemployment

quarterly average, in thousands of persons, in % (rhs)

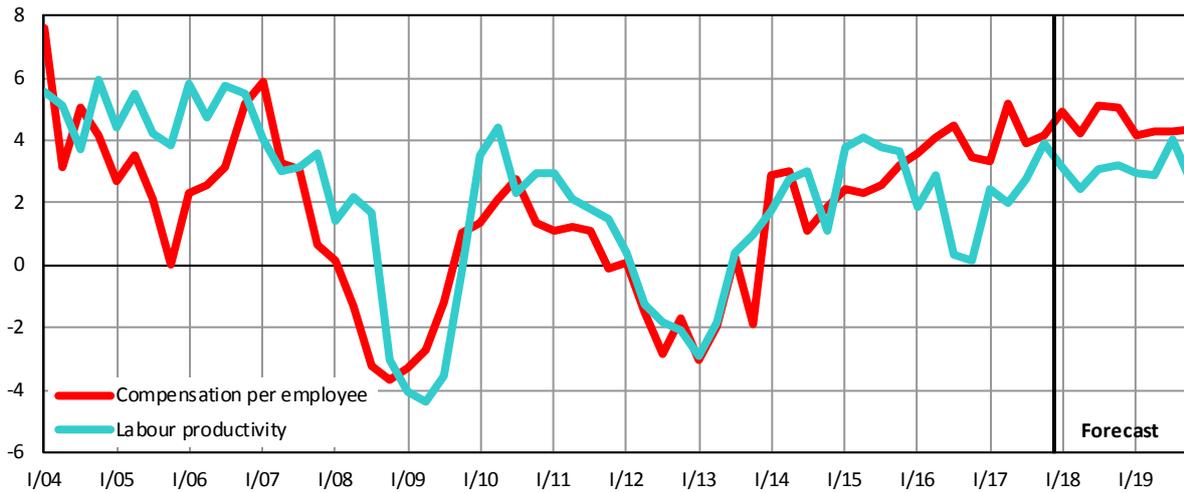


Note: Share of unemployed (Ministry of Labour and Social Affairs) is defined as a share of available job seekers aged 15 to 64 years in the population of the same age.

Source: CZSO, Ministry of Labour and Social Affairs. Calculations of the MoF.

**Graph 3.3.8: Compensation per Employee and Real Productivity of Labour**

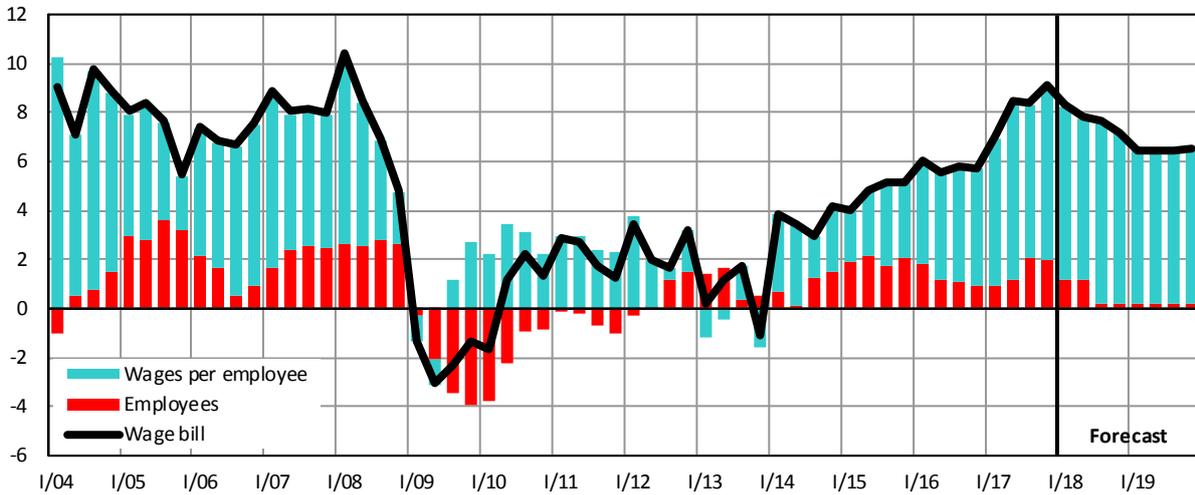
YoY growth rate, in %



Source: CZSO. Calculations of the MoF.

**Graph 3.3.9: Wage Bill – nominal, domestic concept**

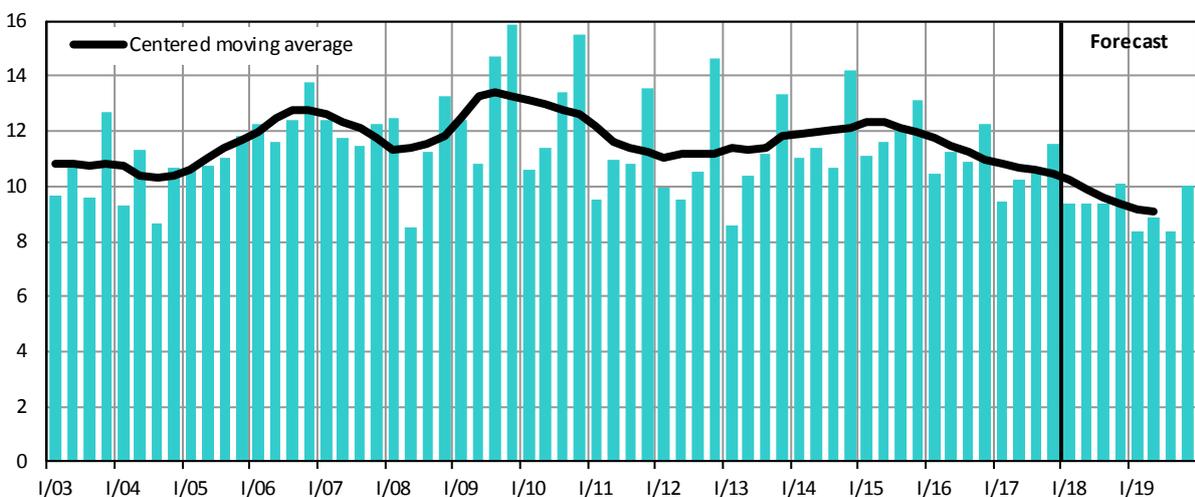
YoY growth rate, in %



Source: CZSO. Calculations of the MoF.

**Graph 3.3.10: Gross Savings Rate of Households**

in % of disposable income



Source: CZSO. Calculations of the MoF.

**Table 3.3.3: Income and Expenditures of Households – yearly**

SNA methodology – national concept

		2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
										Forecast	Forecast
<b>Current income</b>											
<b>Compensation of employees</b>	bill.CZK	<b>1 587</b>	<b>1 627</b>	<b>1 669</b>	<b>1 692</b>	<b>1 760</b>	<b>1 852</b>	<b>1 966</b>	<b>2 128</b>	<b>2 288</b>	<b>2 434</b>
	growth in %	2.2	2.5	2.6	1.3	4.0	5.3	6.1	8.3	7.5	6.4
<b>Gross operating surplus and mixed income</b>	bill.CZK	<b>685</b>	<b>674</b>	<b>654</b>	<b>645</b>	<b>662</b>	<b>691</b>	<b>712</b>	<b>731</b>	<b>757</b>	<b>776</b>
	growth in %	-0.2	-1.7	-2.9	-1.3	2.6	4.3	3.0	2.8	3.5	2.5
<b>Property income received</b>	bill.CZK	<b>154</b>	<b>153</b>	<b>147</b>	<b>158</b>	<b>166</b>	<b>166</b>	<b>158</b>	<b>177</b>	<b>185</b>	<b>194</b>
	growth in %	-2.5	-0.6	-4.0	7.8	5.1	-0.4	-4.6	12.1	4.7	4.9
<b>Social benefits not-in-kind</b>	bill.CZK	<b>541</b>	<b>553</b>	<b>566</b>	<b>563</b>	<b>576</b>	<b>591</b>	<b>606</b>	<b>623</b>	<b>660</b>	<b>705</b>
	growth in %	1.1	2.1	2.4	-0.6	2.2	2.6	2.7	2.7	5.9	6.8
<b>Other current transfers received</b>	bill.CZK	<b>140</b>	<b>139</b>	<b>151</b>	<b>146</b>	<b>160</b>	<b>181</b>	<b>187</b>	<b>224</b>	<b>239</b>	<b>254</b>
	growth in %	-1.0	-0.5	8.6	-3.1	9.2	13.3	3.3	19.6	6.8	6.4
<b>Current expenditure</b>											
<b>Property income paid</b>	bill.CZK	<b>23</b>	<b>21</b>	<b>15</b>	<b>21</b>	<b>16</b>	<b>14</b>	<b>16</b>	<b>16</b>	<b>16</b>	<b>16</b>
	growth in %	17.7	-8.5	-27.2	40.5	-24.3	-10.7	8.0	-0.1	0.7	1.2
<b>Curr. taxes on income and property</b>	bill.CZK	<b>144</b>	<b>156</b>	<b>158</b>	<b>166</b>	<b>177</b>	<b>183</b>	<b>200</b>	<b>216</b>	<b>243</b>	<b>259</b>
	growth in %	-2.5	8.1	1.6	4.9	6.9	3.2	9.2	8.3	12.2	6.8
<b>Social contributions</b>	bill.CZK	<b>621</b>	<b>640</b>	<b>654</b>	<b>670</b>	<b>696</b>	<b>732</b>	<b>775</b>	<b>835</b>	<b>900</b>	<b>956</b>
	growth in %	2.9	3.1	2.3	2.4	3.8	5.3	5.8	7.8	7.7	6.3
<b>Other current transfers paid</b>	bill.CZK	<b>141</b>	<b>145</b>	<b>154</b>	<b>140</b>	<b>150</b>	<b>168</b>	<b>175</b>	<b>215</b>	<b>228</b>	<b>242</b>
	growth in %	-1.6	3.2	6.2	-9.3	6.9	11.9	4.6	22.6	6.1	6.2
<b>Gross disposable income</b>	bill.CZK	<b>2 179</b>	<b>2 184</b>	<b>2 206</b>	<b>2 208</b>	<b>2 285</b>	<b>2 383</b>	<b>2 463</b>	<b>2 601</b>	<b>2 742</b>	<b>2 889</b>
	growth in %	0.8	0.2	1.0	0.1	3.5	4.3	3.4	5.6	5.4	5.3
<b>Final consumption</b>	bill.CZK	<b>1 913</b>	<b>1 952</b>	<b>1 970</b>	<b>1 997</b>	<b>2 044</b>	<b>2 125</b>	<b>2 214</b>	<b>2 358</b>	<b>2 513</b>	<b>2 666</b>
	growth in %	1.5	2.0	0.9	1.3	2.4	3.9	4.2	6.5	6.6	6.1
<b>Change in share in pension funds</b>	bill.CZK	<b>15</b>	<b>16</b>	<b>15</b>	<b>35</b>	<b>35</b>	<b>33</b>	<b>31</b>	<b>32</b>	<b>37</b>	<b>39</b>
<b>Gross savings</b>	bill.CZK	<b>282</b>	<b>248</b>	<b>250</b>	<b>246</b>	<b>276</b>	<b>291</b>	<b>280</b>	<b>276</b>	<b>266</b>	<b>262</b>
<b>Capital transfers</b> (income (-) / expenditure (+))	bill.CZK	<b>-29</b>	<b>-25</b>	<b>-21</b>	<b>-13</b>	<b>-32</b>	<b>-12</b>	<b>-13</b>	<b>-11</b>	<b>-21</b>	<b>-24</b>
<b>Gross capital formation</b>	bill.CZK	<b>230</b>	<b>198</b>	<b>183</b>	<b>181</b>	<b>195</b>	<b>208</b>	<b>223</b>	<b>233</b>	<b>243</b>	<b>252</b>
	growth in %	8.8	-13.9	-7.8	-1.3	8.3	6.6	7.0	4.6	4.2	3.8
<b>Change in financial assets and liab.</b>	bill.CZK	<b>79</b>	<b>73</b>	<b>87</b>	<b>77</b>	<b>110</b>	<b>93</b>	<b>69</b>	<b>53</b>	<b>43</b>	<b>32</b>
<b>Real disposable income</b>	growth in %	<b>0.4</b>	<b>-1.5</b>	<b>-1.2</b>	<b>-0.8</b>	<b>2.9</b>	<b>4.2</b>	<b>2.8</b>	<b>3.1</b>	<b>3.2</b>	<b>3.3</b>
<b>Gross savings rate</b>	%	<b>12.8</b>	<b>11.3</b>	<b>11.3</b>	<b>11.0</b>	<b>11.9</b>	<b>12.1</b>	<b>11.2</b>	<b>10.5</b>	<b>9.6</b>	<b>8.9</b>

Source: CZSO. Calculations of the MoF.

### 3.4 External Relations

The **current account balance to GDP ratio**<sup>2</sup> was 1.1% in the fourth quarter of 2017 (*versus 0.5%*), thus improving by 0.3% of GDP QoQ.

The result for 2017 has to be evaluated in the context of revision of data for 2016 and the first three quarters of 2017, which took place simultaneously with the publication of data for the fourth quarter of 2017. The most significant change for 2016 was a reduction in the surplus on the balance of primary income by 0.4% of GDP to 5.3% of GDP. The current account surplus was thus increased by 0.5% of GDP to 1.6% GDP.

**Export market growth**<sup>3</sup>, which reached 5.6% (*versus 5.4%*) in the fourth quarter of 2017, was faster than estimated. The same growth dynamics were achieved for the entire 2017 (*versus 5.4%*), which is an evidence of strong foreign demand (especially for cars). In view of the forecast slowdown in GDP growth of our main trading partners and the development of their import intensity, we expect the export market growth to slow down to 5.1% (*versus 5.0%*) this year and further to 4.4% (*unchanged*) in 2019.

**Export performance** increased by 2.7% (*versus 1.1%*) in the fourth quarter of 2017. After an increase of 0.6% in 2016, export performance dynamics accelerated to 1.6% in 2017 (*versus 1.2%*). We expect growth in export markets to slow down to 0.6% (*versus 0.5%*) in 2018 and further to 0.5% (*unchanged*) in 2019. Continuing growth in private investments should be reflected favourably in the efficiency of production and, therefore, in the competitiveness of Czech products. The increasing unit labour costs, the appreciation of the koruna and the shortage of workforce will act against a further increase in export performance.

As regards foreign trade (balance of payments methodology), the **balance of goods** deteriorated throughout the last year. According to current data, the balance of goods reached a surplus of 4.8% of GDP (*versus 4.9%*) in 2017. The decreasing surplus was due to factors on the import side. Stronger demand for investment goods led to a higher growth in imports of engineering production, while rising domestic private consumption resulted in higher imports of industrial consumer goods. The dynamic economic growth was also reflected in the increase in imports of semi-finished products and mineral fuels.

Similarly on the export side, growth was seen in commodity classes significant for the Czech economy. According to the standard classification of foreign trade,

the most significant growth in terms of weight was recorded in the machinery and transport (especially automobiles) class, which accounts for more than half of Czech exports and played a major part in the overall balance of goods.

Prices of mineral fuels remain an important factor affecting the **terms of trade** of foreign trade in goods. The fuel balance deficit reached 2.6% of GDP (*versus 2.5%*) in the fourth quarter of 2017. For 2018, we anticipate deepening of the fuel balance deficit to 2.7% of GDP (*versus 2.4%*) following the higher investment activity. In 2019, we expect the fuel balance deficit to decline to 2.5% of GDP (*versus 2.2% of GDP*).

We expect the surplus on the balance of goods to continue to decline and to reach 4.2% of GDP (*versus 4.5% of GDP*) in 2018. For 2019, we expect a further decline in the surplus to 3.8% of GDP (*versus 4.2%*). The deterioration of the forecast for the balance of goods is mainly due to increasing domestic demand (growth in investment activity), expected saturation of demand for cars in Western Europe, and a stronger exchange rate making Czech products more expensive abroad.

The surplus on the **balance of services** has been increasing since the first quarter of 2015. The total surplus on this balance reached 2.4% of GDP (*versus 2.2%*) in 2017. The balances of transportation services, construction works, telecommunication services and IT services have improved in a YoY comparison. With regard to the continuing economic growth we expect improved sales of services abroad in the coming period and the surplus maintained at similar levels. We estimate that the surplus will reach 2.3% of GDP this and in the next year (*versus 2.2% of GDP in both years*).

The lower surplus on the current account in 2017 by 0.5% of GDP YoY was due, in addition to the aforementioned decrease in the surplus on the balance of goods and services by 0.2% of GDP, to deterioration in the **balance of secondary income** by 0.3% of GDP. On the other hand, the deficit of primary income improved YoY by 0.1% of GDP to 5.2% of GDP (*versus 5.4% of GDP*). The improvement was at the expense of a lower growth in profitability of foreign-owned companies in comparison with GDP growth. The primary income item shows a high volatility over time related to the cyclical development of the economy. In spite of persisting pressures on wage growth, and therefore a shift of distribution of GDP from net corporate profit to compensation of employees, companies under foreign control show profitability growth. Therefore, we expect the deficit of primary income to remain almost unchanged in the following two years. In 2018, it could reach 5.2% of GDP (*versus 5.3% of GDP*), and we expect a deficit of 5.1% of GDP (*versus 5.3%*) in 2019.

<sup>2</sup> All the *quarterly* figures relative to GFP are listed in annual moving totals.

<sup>3</sup> In 2017, the most important trading partners included Germany with a 32.2% share in Czech exports, Slovakia with 9.0%, Poland with 6.4%, France with 5.1%, the United Kingdom with 4.8%, and Austria with 4.4%.

In this context, we estimate that the **current account of the balance of payments** will show a moderate surplus of 0.4% GDP in 2018 (*versus 0.1%*). For 2019, we expect

a further decline in the positive balance to 0.2% of GDP (*versus 0.1%*).

### Box 3.1: Foreign Investments in the CR and Outflow of Profits

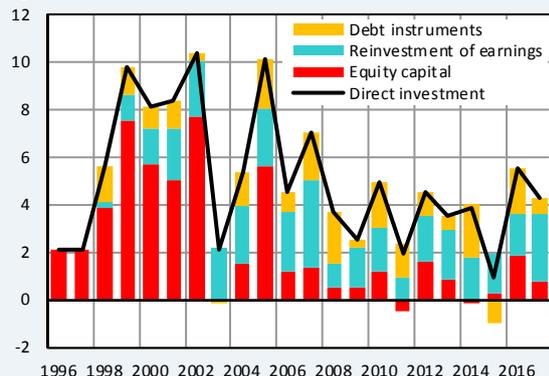
Attention of the public discussion has been lately paid to the issue of outflow of profits from the Czech economy. In 2017, the outflow of income from foreign direct investments was CZK 397 billion, CZK 27 billion from portfolio investments and CZK 15 billion from other investments. The YoY increase in outflow of income from investments reached 3.5%; it was 5.0% in the case of income from foreign direct investments. Given the size of the phenomenon, this box deals with the issue of outflow of income from foreign direct investments in the context of developments of the Czech economy.

The inflow of foreign direct investments to the CR corresponds to the current average position in the investment cycle (Graph 1). With respect to low domestic capital, large amounts were invested in the first phase (import of foreign direct investments). In the second phase, the foreign direct investments were reflected in the production and export growth, and reinvestment grew. Finally, in the third phase, foreign capital owners are paid higher dividends with the growing profitability of foreign companies (growth in production and value added enhanced exports and growth in incomes). The inflow of new foreign direct investments to the CR has thus been gradually declining in relation to GDP, and the reinvested earnings ratio remains relatively stable.

Foreign investments significantly transformed the Czech economy mainly in the second half of the 1990s in the area of retail and emerging mobile communications. The Investment Incentive Act was adopted in 2000, which accelerated the inflow of investments from abroad for a short time.<sup>4</sup> The Investment Incentive Act was amended in the subsequent years, though until 2012 the system of investment incentives only applied to manufacturing. The ratio of the stock of foreign investments in manufacturing to GDP increased from 13% to 21% in that period (Graph 2). In 2012, support for investment incentives was extended to technology centres and strategic services centres.

**Graph 1: Structure of FDI Inflows to the Czech Republic**

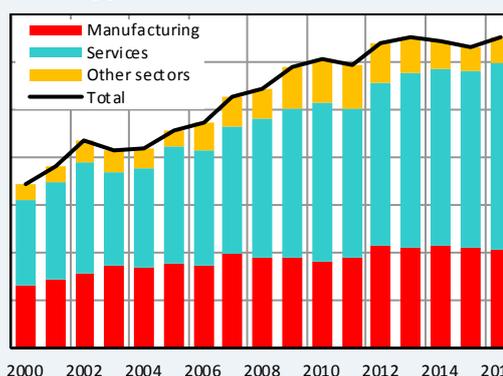
in % of GDP



Source: CNB, CZSO. Calculations of the MoF.

**Graph 2: Sectoral Breakdown of FDI**

in % of GDP, end-of-period data



Note: Only data up to the year 2016 were available.

Source: CNB, CZSO. Calculations of the MoF.

The inflow of foreign capital had positive macroeconomic impacts. Graph 3 shows an increase in value added of foreign-owned non-financial corporations in the years of highest inflows of foreign direct investments. Foreign production procedures and know-how stimulated the value added of the Czech economy, leading at the same time to higher involvement of domestic companies in international supply chains.

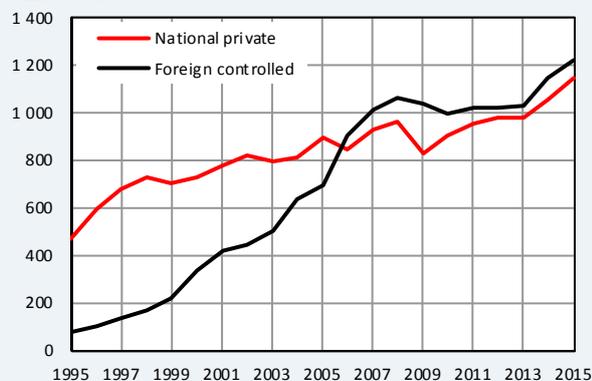
Newly created capacities with the participation of foreign capital were largely export-oriented. After the initial increased demand of realized investments for imports (import of technologies), their export potential prevailed, and a surplus on the balance of goods was achieved in 2005 for the first time in the history of the CR; it increased over time to 4.8% of GDP in 2017. A strong focus on the automotive industry has led to the fact that the Czech Republic with its production of 1.41 million cars was the 13th largest producer of passenger cars on the global scale in 2017, overtaking even much larger traditional producers such as Russia or Italy. On the other hand, the high dependence of the Czech economy on the automotive industry can be legitimately perceived as a risk factor especially in the case of a decline in foreign demand. Manufacture of motor vehicles in 2016 accounted for 5.6% of the gross value added, but the share of the automotive industry in the economy was higher due to associated production in other industries. The share of motor vehicles in exports of goods was 28.5% in 2017 (according to foreign trade statistics in the national concept).

<sup>4</sup> Besides the investment incentives, the CR's accession to the EU in 2004 contributed positively to the inflow of foreign direct investment.

The impact of foreign investments on the domestic economy can be illustrated also through operating profitability (Graph 4), i.e. the ratio of gross operating surplus to net assets of domestic and foreign enterprises. In the second half of the 1990s, domestic private non-financial corporations achieved significantly higher profitability than foreign-controlled enterprises. The lower profitability of foreign companies is due to higher costs of the implementation of investment activities in the Czech Republic. Since 2001 there has been an increase in the profitability of foreign-controlled enterprises, but over time, as a result of the international movement of capital and the spillover effect (economic convergence), the profitability of domestic and foreign companies became equal.

**Graph 3: GVA of Non-Financial Firms by Type of Ownership**

in CZK billion

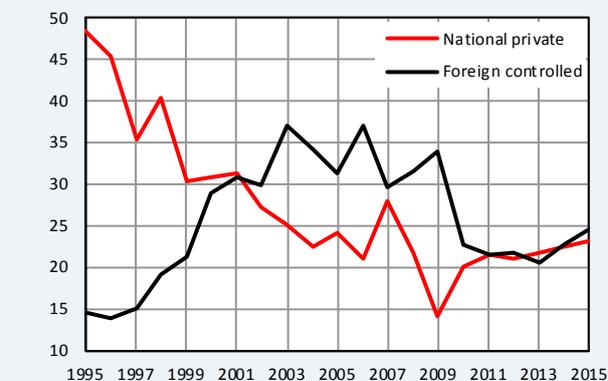


Note: Only data up to the year 2015 were available.

Source: CZSO. Calculations of the MoF.

**Graph 4: Operating Profitability of Non-Financial Firms**

in %



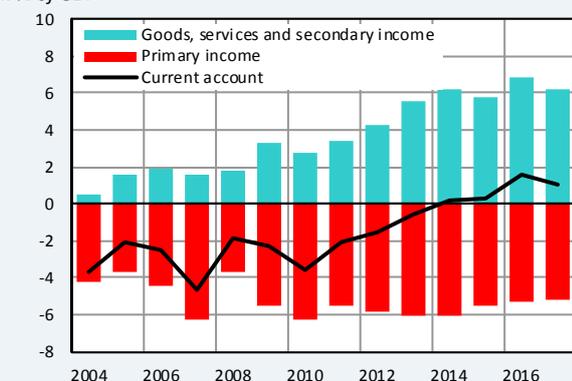
Note: Only data up to the year 2015 were available.

Source: CZSO. Calculations of the MoF.

The “price” for the final phase of foreign direct investment became the increasing deficit on the balance of primary income (Graph 5) within the current account of the balance of payments, which was 5.2% of GDP in 2017. The crucial item is the investment income deficit (6.4% of GDP), mainly due to the direct investment income deficit (6.8% of GDP). The main part of this item (Graph 6) consists of dividends (4.5% of GDP), and one third of the deficit is due to reinvested earnings (2.1% of GDP).

**Graph 5: Breakdown of the Current Account of the BoP**

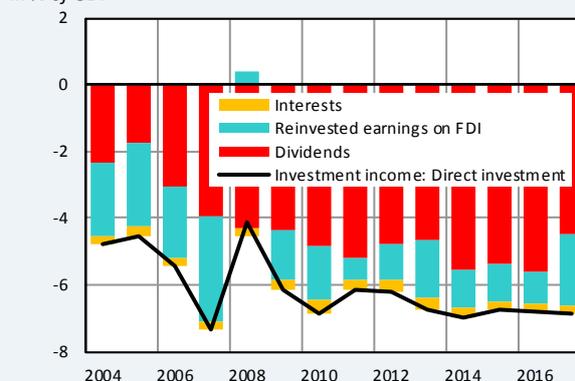
in % of GDP



Source: CNB, CZSO. Calculations of the MoF.

**Graph 6: Breakdown of FDI Income (Balance)**

in % of GDP



Source: CNB, CZSO. Calculations of the MoF.

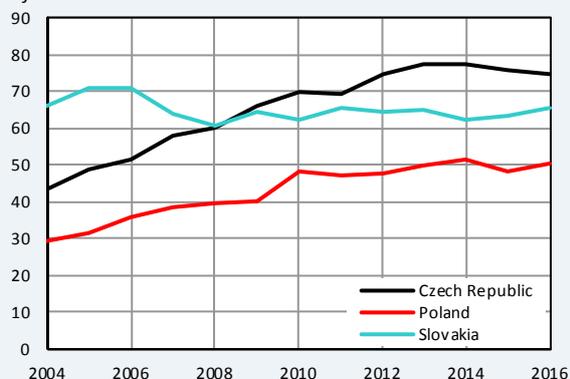
The deficit of primary income has to be viewed as a profit from the newly created value that was produced by foreign entities operating in the Czech Republic. The outflow of income from foreign direct investments is only a consequence of the previous inflow of foreign capital. The inflow of capital to the CR also benefits the domestic labour force, whose labour productivity and ultimately real wages increase thanks to higher capital endowment. Therefore, the convergence process accelerates with the inflow of capital.

Methodical treatment is an important aspect. Apart from dividends, the balance on the current account of the balance of payments also includes reinvested earnings as a part of foreign direct investments. Reinvested earnings, however, are recorded as outflow of funds on the current account and at the same time as inflow on the financial account within foreign direct investments. In countries where reinvested earnings account for a large share of foreign direct investment inflow (67% in the Czech Republic in 2017), the current account deficit increases (or a surplus decreases) without actual cash flows with foreign entities taking place (Graph 7).

In international comparison of countries that have also undergone the transformation process, the Czech Republic shows a higher level of foreign direct investments relative to GDP (Graph 8). However, since 2014, there is a downward trend in investment inflow, which may be linked to increased capacity utilization and higher investment opportunities abroad, but this development may at the same time be a sign of replacement of foreign investments with domestic ones. On the other hand, there is a higher outflow of dividends compared to Poland and Slovakia (Graph 9), which is to a certain extent due to a high level of foreign direct investment compared to the neighbouring countries. At the same time, the Czech Republic shows a higher reinvested earnings to GDP ratio (in 2017, this ratio was 2.9% of GDP in the CR, 1.2% of GDP in Slovakia, and 1.6% of GDP in Poland). This indicates a higher ability to finance investment projects from foreign companies' profits, which is also indicated by an increase in the share of reinvested earnings in total investment (Graph 1).

**Graph 8: FDI in Selected Countries<sup>5</sup>**

in % of GDP

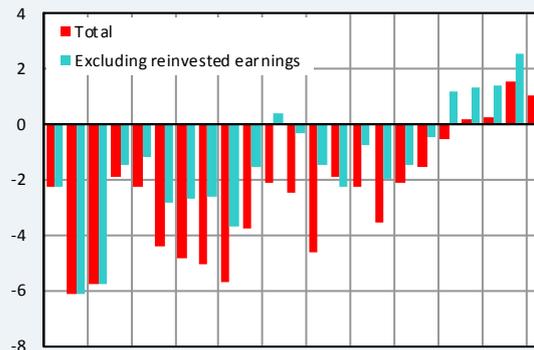


Note: Only data up to the year 2016 were available.

Source: Eurostat.

**Graph 7: Current Account Balance**

in % of GDP

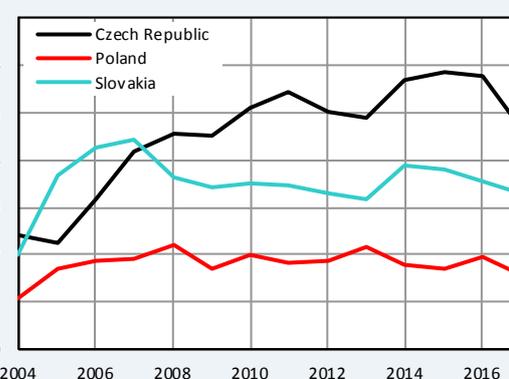


1995 1997 1999 2001 2003 2005 2007 2009 2011 2013 2015 2017

Source: CNB, CZSO. Calculations of the MoF.

**Graph 9: Outflows of Dividends from FDI**

in % of GDP



Source: Eurostat, CNB, Národná banka Slovenska, Narodowy Bank Polski. Calculations of the MoF.

<sup>5</sup> The stock of foreign direct investment reported within international comparison differs from that reported by the CNB and shown in Graph 2. The reason is a different methodical treatment of loan flows from direct investments. Whereas the methodology used by the CNB captures the stock of foreign investment after the deduction of loan repayments, the Eurostat's methodology is based on stocks before the deduction of loan repayments. With respect to international comparability, the Eurostat's methodology of reporting foreign direct investments is used in the text.

**Table 3.4.1: Balance of Payments – yearly**

		2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
										Forecast	Forecast
<b>Goods and services</b>	<i>bill.CZK</i>	119	157	201	237	276	266	353	363	346	342
	<i>% GDP</i>	<b>3.0</b>	<b>3.9</b>	<b>5.0</b>	<b>5.8</b>	<b>6.4</b>	<b>5.8</b>	<b>7.4</b>	<b>7.2</b>	<b>6.5</b>	<b>6.1</b>
Goods	<i>bill.CZK</i>	40	75	124	167	220	188	246	241	222	214
	<i>% GDP</i>	<b>1.0</b>	<b>1.9</b>	<b>3.0</b>	<b>4.1</b>	<b>5.1</b>	<b>4.1</b>	<b>5.1</b>	<b>4.8</b>	<b>4.2</b>	<b>3.8</b>
Services	<i>bill.CZK</i>	78	81	78	70	56	78	108	122	124	129
	<i>% GDP</i>	<b>2.0</b>	<b>2.0</b>	<b>1.9</b>	<b>1.7</b>	<b>1.3</b>	<b>1.7</b>	<b>2.3</b>	<b>2.4</b>	<b>2.3</b>	<b>2.3</b>
<b>Primary income</b>	<i>bill.CZK</i>	-250	-223	-238	-249	-261	-255	-252	-261	-275	-284
	<i>% GDP</i>	<b>-6.3</b>	<b>-5.5</b>	<b>-5.9</b>	<b>-6.1</b>	<b>-6.0</b>	<b>-5.5</b>	<b>-5.3</b>	<b>-5.2</b>	<b>-5.2</b>	<b>-5.1</b>
<b>Secondary income</b>	<i>bill.CZK</i>	-11	-18	-27	-10	-7	0	-27	-48	-52	-49
	<i>% GDP</i>	<b>-0.3</b>	<b>-0.5</b>	<b>-0.7</b>	<b>-0.2</b>	<b>-0.2</b>	<b>0.0</b>	<b>-0.6</b>	<b>-0.9</b>	<b>-1.0</b>	<b>-0.9</b>
<b>Current account</b>	<i>bill.CZK</i>	-142	-85	-63	-22	8	11	74	54	19	9
	<i>% GDP</i>	<b>-3.6</b>	<b>-2.1</b>	<b>-1.6</b>	<b>-0.5</b>	<b>0.2</b>	<b>0.2</b>	<b>1.6</b>	<b>1.1</b>	<b>0.4</b>	<b>0.2</b>
<b>Capital account</b>	<i>bill.CZK</i>	38	13	53	82	32	102	54	46	54	62
	<i>% GDP</i>	<b>0.9</b>	<b>0.3</b>	<b>1.3</b>	<b>2.0</b>	<b>0.7</b>	<b>2.2</b>	<b>1.1</b>	<b>0.9</b>	<b>1.0</b>	<b>1.1</b>
<b>Net lending/borrowing</b>	<i>bill.CZK</i>	-104	-72	-10	61	40	113	128	101	74	72
	<i>% GDP</i>	<b>-2.6</b>	<b>-1.8</b>	<b>-0.3</b>	<b>1.5</b>	<b>0.9</b>	<b>2.5</b>	<b>2.7</b>	<b>2.0</b>	<b>1.4</b>	<b>1.3</b>
<b>Financial account</b>	<i>bill.CZK</i>	-122	-75	12	68	64	175	117	117	.	.
Direct investments	<i>bill.CZK</i>	-95	-47	-121	7	-80	50	-187	-135	.	.
Portfolio investments	<i>bill.CZK</i>	-150	-6	-55	-93	90	-164	-170	-268	.	.
Financial derivatives	<i>bill.CZK</i>	5	4	-9	-5	-6	-5	11	-14	.	.
Other investments	<i>bill.CZK</i>	77	-9	116	-30	-13	-57	-102	-712	.	.
Reserve assets	<i>bill.CZK</i>	41	-17	80	188	73	351	564	1 246	.	.
<b>International investment position</b>	<i>bill.CZK</i>	-1 823	-1 823	-1 864	-1 695	-1 577	-1 513	-1 283	-1 337	.	.
	<i>% GDP</i>	<b>-46.0</b>	<b>-45.2</b>	<b>-45.9</b>	<b>-41.4</b>	<b>-36.6</b>	<b>-32.9</b>	<b>-26.9</b>	<b>-26.4</b>	.	.
<b>Gross external debt</b>	<i>bill.CZK</i>	2 164	2 312	2 434	2 733	2 947	3 119	3 498	4 372	.	.
	<i>% GDP</i>	<b>54.6</b>	<b>57.3</b>	<b>60.0</b>	<b>66.7</b>	<b>68.3</b>	<b>67.9</b>	<b>73.3</b>	<b>86.5</b>	.	.

Source: CNB, CZSO. Calculations of the MoF.

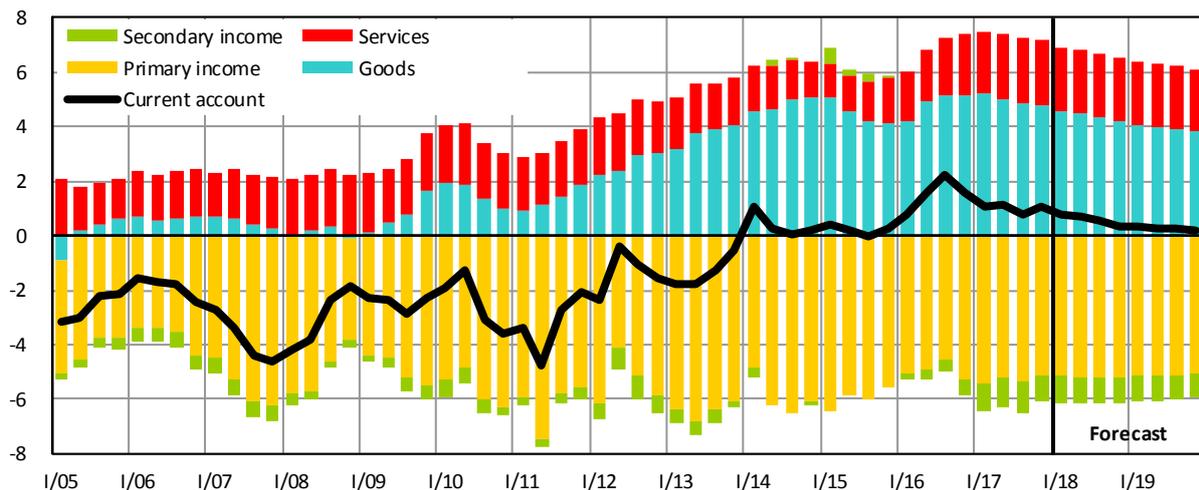
**Table 3.4.2: Balance of Payments – quarterly**  
moving sums of the latest 4 quarters

		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
						<i>Estimate</i>	<i>Forecast</i>	<i>Forecast</i>	<i>Forecast</i>
<b>Goods and services</b>	<i>bill.CZK</i>	362	360	361	363	354	355	351	346
	<i>% GDP</i>	<b>7.5</b>	<b>7.4</b>	<b>7.3</b>	<b>7.2</b>	<b>6.9</b>	<b>6.8</b>	<b>6.7</b>	<b>6.5</b>
Goods	<i>bill.CZK</i>	251	243	241	241	233	233	228	222
	<i>% GDP</i>	<b>5.2</b>	<b>5.0</b>	<b>4.9</b>	<b>4.8</b>	<b>4.5</b>	<b>4.5</b>	<b>4.3</b>	<b>4.2</b>
Services	<i>bill.CZK</i>	111	118	120	122	121	122	123	124
	<i>% GDP</i>	<b>2.3</b>	<b>2.4</b>	<b>2.4</b>	<b>2.4</b>	<b>2.4</b>	<b>2.4</b>	<b>2.3</b>	<b>2.3</b>
<b>Primary income</b>	<i>bill.CZK</i>	-261	-253	-263	-261	-264	-268	-272	-275
	<i>% GDP</i>	<b>-5.4</b>	<b>-5.2</b>	<b>-5.3</b>	<b>-5.2</b>	<b>-5.2</b>	<b>-5.2</b>	<b>-5.2</b>	<b>-5.2</b>
<b>Secondary income</b>	<i>bill.CZK</i>	-49	-53	-59	-48	-49	-50	-51	-52
	<i>% GDP</i>	<b>-1.0</b>	<b>-1.1</b>	<b>-1.2</b>	<b>-0.9</b>	<b>-1.0</b>	<b>-1.0</b>	<b>-1.0</b>	<b>-1.0</b>
<b>Current account</b>	<i>bill.CZK</i>	52	54	39	54	41	37	29	19
	<i>% GDP</i>	<b>1.1</b>	<b>1.1</b>	<b>0.8</b>	<b>1.1</b>	<b>0.8</b>	<b>0.7</b>	<b>0.5</b>	<b>0.4</b>
<b>Capital account</b>	<i>bill.CZK</i>	36	22	18	46	48	50	52	54
	<i>% GDP</i>	<b>0.7</b>	<b>0.5</b>	<b>0.4</b>	<b>0.9</b>	<b>0.9</b>	<b>1.0</b>	<b>1.0</b>	<b>1.0</b>
<b>Net lending/borrowing</b>	<i>bill.CZK</i>	88	76	57	101	89	87	81	74
	<i>% GDP</i>	<b>1.8</b>	<b>1.6</b>	<b>1.1</b>	<b>2.0</b>	<b>1.7</b>	<b>1.7</b>	<b>1.5</b>	<b>1.4</b>
<b>Financial account</b>	<i>bill.CZK</i>	89	134	135	117	.	.	.	.
Direct investments	<i>bill.CZK</i>	-247	-178	-127	-135	.	.	.	.
Portfolio investments	<i>bill.CZK</i>	-479	-464	-363	-268	.	.	.	.
Financial derivatives	<i>bill.CZK</i>	11	6	-2	-14	.	.	.	.
Other investments	<i>bill.CZK</i>	-728	-815	-804	-712	.	.	.	.
Reserve assets	<i>bill.CZK</i>	1 532	1 586	1 430	1 246	.	.	.	.
<b>International investment position</b>	<i>stock in bill.CZK</i>	-1 023	-1 193	-1 250	-1 337	.	.	.	.
	<i>% GDP</i>	<b>-21.2</b>	<b>-24.5</b>	<b>-25.2</b>	<b>-26.4</b>	.	.	.	.
<b>Gross external debt</b>	<i>stock in bill.CZK</i>	4 347	4 397	4 438	4 372	.	.	.	.
	<i>% GDP</i>	<b>90.1</b>	<b>90.2</b>	<b>89.5</b>	<b>86.5</b>	.	.	.	.

Source: CNB, CZSO. Calculations of the MoF.

**Graph 3.4.1: Current Account**

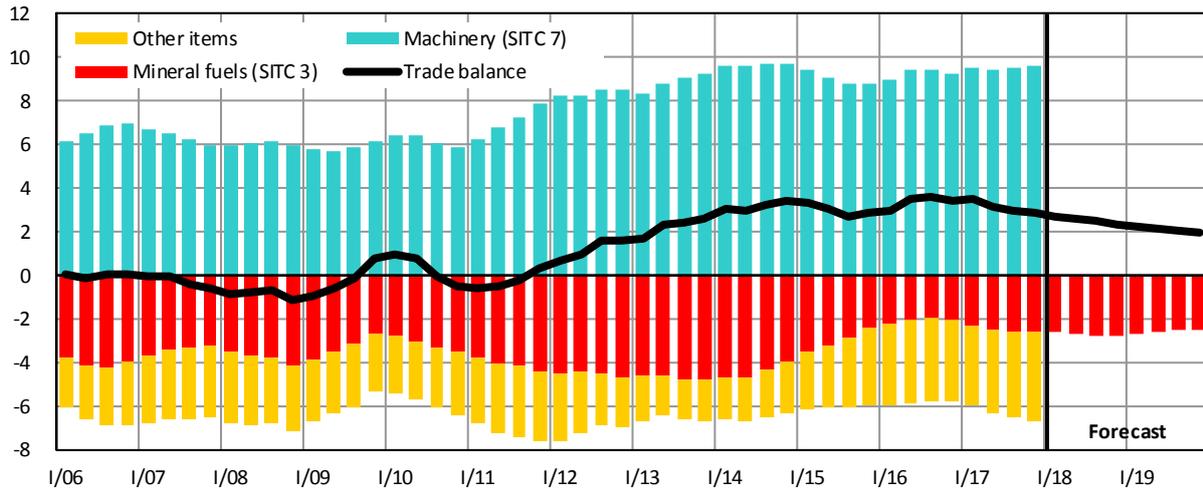
moving sums of the latest 4 quarters, in % of GDP, trade and service balances in BoP definitions



Source: CNB, CZSO. Calculations of the MoF.

### Graph 3.4.2: Balance of Trade (national concept)

moving sums of the latest 4 quarters, in % of GDP, in cross-border definitions

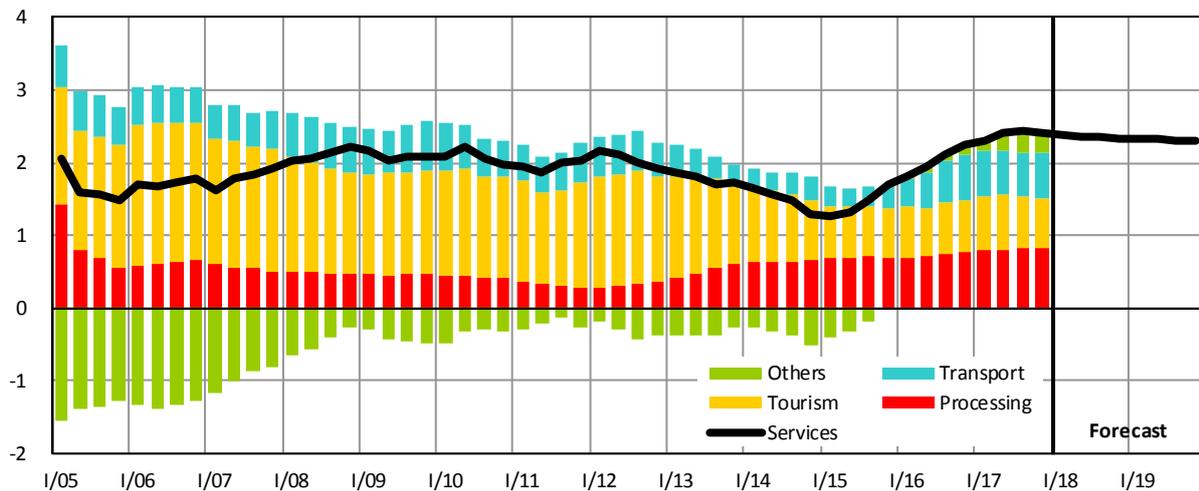


Note: The data in the graph show imports in cif methodology. For this reason, the graph is not comparable with Tables 3.4.1 and 3.4.2, where imports are in fob methodology. Trade balance in the national concept (unlike in the BoP methodology in Tables 3.4.1 and 3.4.2) does not include the import of JAS-39 Gripen fighter jets in the fourth quarter of 2015 amounting to CZK 9.9 bill., i.e. 0.2% of GDP.

Source: CZSO. Calculations of the MoF.

### Graph 3.4.3: Balance of Services

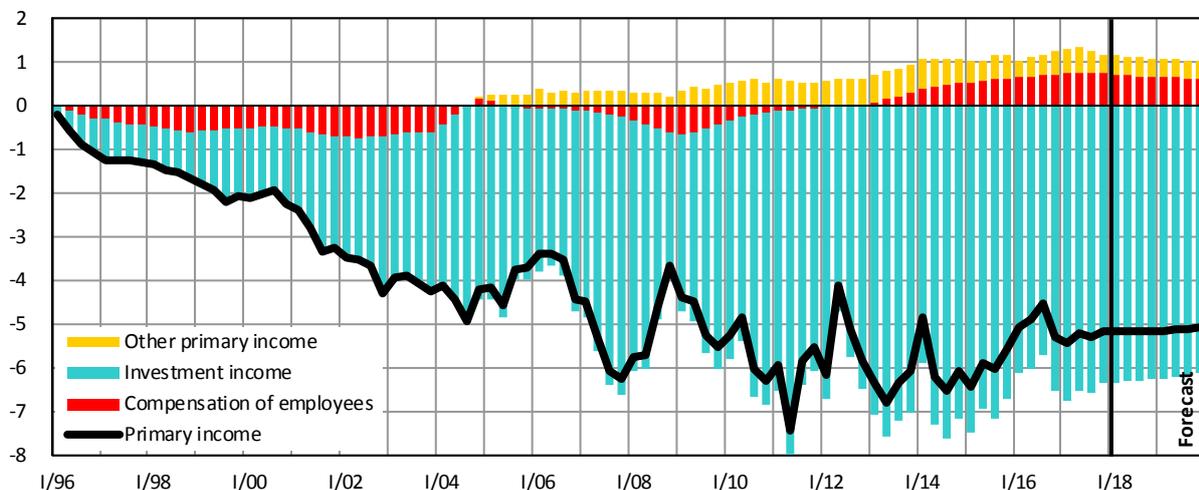
moving sums of the latest 4 quarters, in % of GDP



Source: CNB, CZSO. Calculations of the MoF.

### Graph 3.4.4: Balance of Primary Income

moving sums of the latest 4 quarters, in % of GDP



Source: CNB, CZSO. Calculations of the MoF.

**Table 3.4.3: Decomposition of Exports of Goods – yearly***seasonally adjusted*

		2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	
											<i>Forecast</i>	<i>Forecast</i>
<b>GDP</b> <sup>1)</sup>	<i>average of 2005=100</i>	100.0	103.4	104.4	105.3	107.5	109.8	112.1	115.3	118	121	
	<i>growth in %</i>	<b>3.6</b>	<b>3.4</b>	<b>1.0</b>	<b>0.9</b>	<b>2.1</b>	<b>2.1</b>	<b>2.1</b>	<b>2.8</b>	<b>2.6</b>	<b>2.4</b>	
<b>Import intensity</b> <sup>2)</sup>	<i>average of 2005=100</i>	100.0	104.0	103.1	104.5	107.2	110.4	112.1	115.1	118	120	
	<i>growth in %</i>	<b>8.7</b>	<b>4.0</b>	<b>-0.9</b>	<b>1.4</b>	<b>2.6</b>	<b>3.0</b>	<b>1.5</b>	<b>2.7</b>	<b>2.4</b>	<b>1.9</b>	
<b>Export markets</b> <sup>3)</sup>	<i>average of 2005=100</i>	100.0	107.5	107.6	110.0	115.3	121.2	125.7	132.7	139	146	
	<i>growth in %</i>	<b>12.6</b>	<b>7.5</b>	<b>0.1</b>	<b>2.3</b>	<b>4.8</b>	<b>5.1</b>	<b>3.7</b>	<b>5.6</b>	<b>5.1</b>	<b>4.4</b>	
<b>Export performance</b>	<i>average of 2005=100</i>	100.0	102.5	106.9	105.2	109.6	109.9	110.6	112.4	113	114	
	<i>growth in %</i>	<b>2.5</b>	<b>2.5</b>	<b>4.3</b>	<b>-1.6</b>	<b>4.3</b>	<b>0.3</b>	<b>0.6</b>	<b>1.6</b>	<b>0.6</b>	<b>0.5</b>	
<b>Real exports</b>	<i>average of 2005=100</i>	100.0	110.2	115.0	115.7	126.4	133.3	139.1	149.1	158	165	
	<i>growth in %</i>	<b>15.4</b>	<b>10.2</b>	<b>4.4</b>	<b>0.6</b>	<b>9.2</b>	<b>5.4</b>	<b>4.3</b>	<b>7.2</b>	<b>5.7</b>	<b>4.9</b>	
<b>1 / NEER</b>	<i>average of 2005=100</i>	100.0	97.0	101.3	103.0	108.6	109.9	106.9	103.9	98	96	
	<i>growth in %</i>	<b>-2.2</b>	<b>-3.0</b>	<b>4.4</b>	<b>1.7</b>	<b>5.5</b>	<b>1.2</b>	<b>-2.8</b>	<b>-2.8</b>	<b>-5.5</b>	<b>-1.9</b>	
<b>Prices on foreign markets</b>	<i>average of 2005=100</i>	100.0	103.9	102.8	102.6	101.0	98.4	98.2	99.9	102	104	
	<i>growth in %</i>	<b>1.0</b>	<b>3.9</b>	<b>-1.1</b>	<b>-0.1</b>	<b>-1.6</b>	<b>-2.6</b>	<b>-0.1</b>	<b>1.7</b>	<b>1.9</b>	<b>1.8</b>	
<b>Exports deflator</b>	<i>average of 2005=100</i>	100.0	100.8	104.0	105.7	109.7	108.2	105.0	103.8	100	100	
	<i>growth in %</i>	<b>-1.2</b>	<b>0.8</b>	<b>3.2</b>	<b>1.5</b>	<b>3.8</b>	<b>-1.4</b>	<b>-2.9</b>	<b>-1.2</b>	<b>-3.7</b>	<b>-0.2</b>	
<b>Nominal exports</b>	<i>average of 2005=100</i>	100.0	111.0	119.6	122.3	138.6	144.1	146.0	154.7	157	165	
	<i>growth in %</i>	<b>14.2</b>	<b>11.0</b>	<b>7.8</b>	<b>2.2</b>	<b>13.4</b>	<b>4.0</b>	<b>1.3</b>	<b>5.9</b>	<b>1.8</b>	<b>4.8</b>	

<sup>1)</sup> Weighted average of GDP of the seven most important partners – Germany, Slovakia, Austria, the United Kingdom, Poland, France and Italy.<sup>2)</sup> Index of ratio of real imports of goods to real GDP.<sup>3)</sup> Weighted average of imports of goods of the main partners.

Source: CNB, CZSO, Eurostat. Calculations of the MoF.

**Table 3.4.4: Decomposition of Exports of Goods – quarterly***seasonally adjusted*

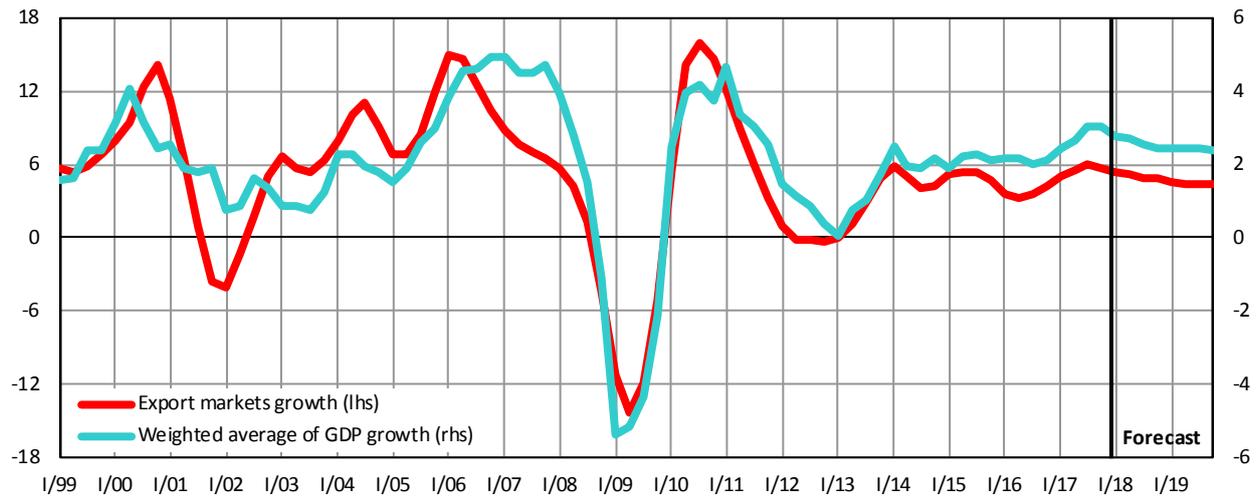
		2017				2018			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
						<i>Estimate</i>	<i>Forecast</i>	<i>Forecast</i>	<i>Forecast</i>
<b>GDP</b> <sup>1)</sup>	<i>average of 2010=100</i>	114.0	114.8	115.7	116.5	117	118	119	119
	<i>growth in %</i>	<b>2.5</b>	<b>2.6</b>	<b>3.0</b>	<b>3.0</b>	<b>2.8</b>	<b>2.7</b>	<b>2.5</b>	<b>2.4</b>
<b>Import intensity</b> <sup>2)</sup>	<i>average of 2010=100</i>	114.0	114.8	115.6	116.1	117	118	118	119
	<i>growth in %</i>	<b>2.4</b>	<b>2.9</b>	<b>3.0</b>	<b>2.5</b>	<b>2.6</b>	<b>2.5</b>	<b>2.2</b>	<b>2.3</b>
<b>Export markets</b> <sup>3)</sup>	<i>average of 2010=100</i>	130.0	131.8	133.7	135.2	137	139	140	142
	<i>growth in %</i>	<b>5.0</b>	<b>5.6</b>	<b>6.1</b>	<b>5.6</b>	<b>5.4</b>	<b>5.3</b>	<b>4.9</b>	<b>4.8</b>
<b>Export performance</b>	<i>average of 2010=100</i>	111.7	114.6	111.0	112.2	113	115	112	113
	<i>growth in %</i>	<b>-0.8</b>	<b>2.7</b>	<b>1.6</b>	<b>2.7</b>	<b>1.0</b>	<b>0.5</b>	<b>0.5</b>	<b>0.5</b>
<b>Real exports</b>	<i>average of 2010=100</i>	145.2	151.0	148.5	151.7	155	160	156	160
	<i>growth in %</i>	<b>4.1</b>	<b>8.4</b>	<b>7.8</b>	<b>8.5</b>	<b>6.4</b>	<b>5.8</b>	<b>5.4</b>	<b>5.3</b>
<b>1 / NEER</b>	<i>average of 2010=100</i>	107.4	105.3	102.2	100.6	99	98	98	97
	<i>growth in %</i>	<b>0.5</b>	<b>-1.5</b>	<b>-4.3</b>	<b>-6.0</b>	<b>-7.7</b>	<b>-6.5</b>	<b>-4.3</b>	<b>-3.4</b>
<b>Prices on foreign markets</b>	<i>average of 2010=100</i>	99.4	99.5	100.1	100.6	102	101	102	102
	<i>growth in %</i>	<b>1.1</b>	<b>1.7</b>	<b>2.0</b>	<b>2.1</b>	<b>2.2</b>	<b>1.8</b>	<b>1.8</b>	<b>1.8</b>
<b>Exports deflator</b>	<i>average of 2010=100</i>	106.8	104.7	102.4	101.2	101	100	100	100
	<i>growth in %</i>	<b>1.5</b>	<b>0.2</b>	<b>-2.3</b>	<b>-4.0</b>	<b>-5.7</b>	<b>-4.8</b>	<b>-2.6</b>	<b>-1.7</b>
<b>Nominal exports</b>	<i>average of 2010=100</i>	155.0	158.1	152.0	153.5	156	159	156	159
	<i>growth in %</i>	<b>5.7</b>	<b>8.6</b>	<b>5.2</b>	<b>4.2</b>	<b>0.4</b>	<b>0.7</b>	<b>2.6</b>	<b>3.6</b>

See notes to Table 3.4.3.

Source: CNB, CZSO, Eurostat. Calculations of the MoF.

### Graph 3.4.5: GDP and Imports of Goods in Main Partner Countries

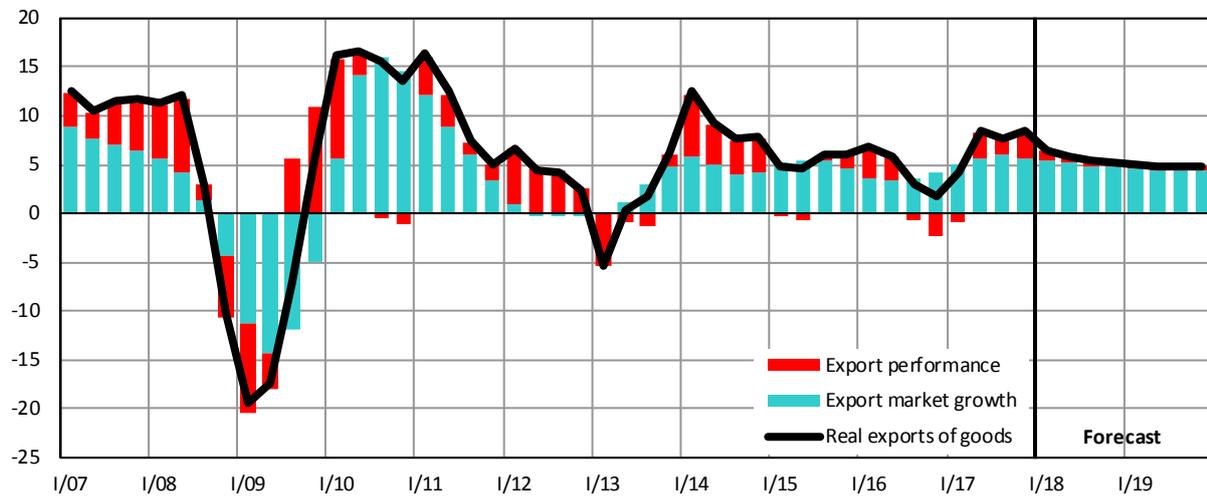
YoY growth rate, in %, seasonally adjusted



Source: Eurostat. Calculations of the MoF.

### Graph 3.4.6: Real Exports of Goods

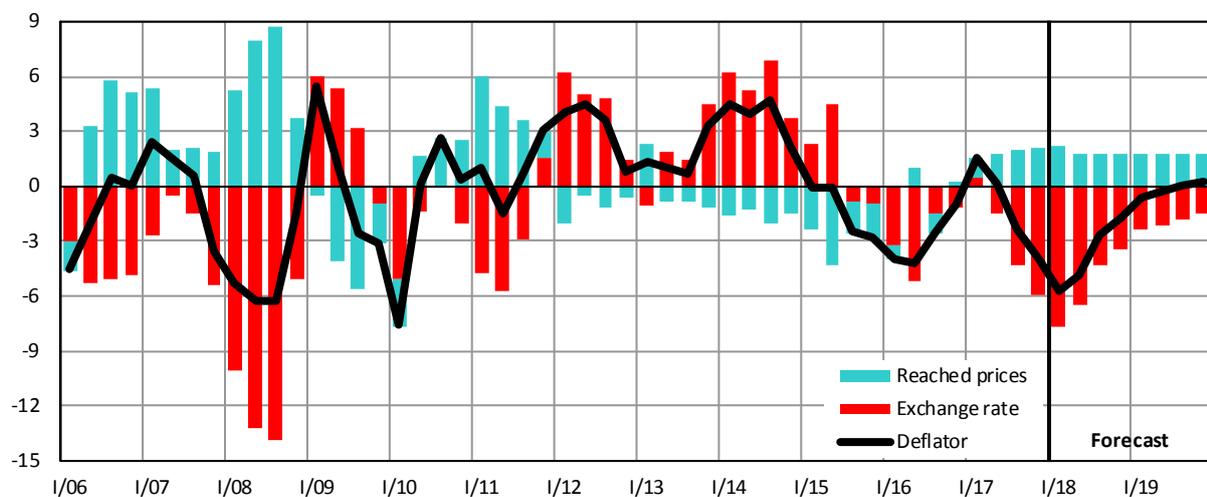
decomposition of YoY growth, in %, seasonally adjusted



Source: CZSO, Eurostat. Calculations of the MoF.

### Graph 3.4.7: Deflator of Exports of Goods

decomposition of YoY growth, in %



Source: CNB, CZSO. Calculations of the MoF.

### 3.5 International Comparisons

Comparisons for the period up to and including 2016 are based on Eurostat statistics. Since 2017, our own calculations on the basis of real exchange rates have been used.

GDP per capita in **current purchasing power parity** increased in most of the monitored countries in 2016; a slight decrease in both absolute and relative terms compared to the EA19 was recorded in Greece due to a fall in economic output. The relative economic level, however, decreased also in Hungary. In the Czech Republic, the purchasing power parity was 17.66 CZK/PPS compared to the EU28 and 17.27 CZK/EUR compared to the EA19. The economic level was approx. 25,600 PPS, corresponding to 82% of the economic level in the EA19. The relative economic level of the Czech Republic should increase gradually up to 87% of the EA19 average in 2019, thanks to the continued economic growth.

GDP per capita, recalculated using the current **exchange rate**, was approx. 16,700 EUR in the CR in 2016, i.e. 53% of the EA19 level. Higher economic growth and the exchange rate appreciation will result in a gradual increase in the relative level up to 61% of the EA19 average in 2019.

As for the comparison of price levels, the **comparative price level of GDP** in the Czech Republic again slightly increased in 2016, reaching 64% of the EA19 average. We expect that the comparative price level of GDP should gradually increase to the level of 70% of the EA19 average in 2019. However, this increase should not jeopardize the competitiveness of the Czech economy.

Through the decomposition<sup>6</sup> of GDP per capita into individual components (labour productivity, labour market component and demographic component) it is possible to determine in detail the sources of economic growth. The results of the analysis are summarised in Graphs 3.5.5 and 3.5.6.

**Labour productivity** measured as the GDP/hours worked ratio has long been increasing in the monitored countries; however, its level is still relatively low compared to

the EA19 average. Although the economic crisis slowed down labour productivity growth, its absolute level did not decrease in 2008–2016 in any of the monitored countries except Greece. In the given period, however, a decrease in the relative level of labour productivity with respect to the EA19 countries was also seen, in addition to Greece, in Slovenia and Portugal, whereas the relative levels increased approximately by 8 pp in Poland and Latvia. Given that the growth rate of hours worked was higher than of GDP in current purchasing power parity, labour productivity in the Czech Republic decreased by 1.2% in 2016, reaching 66% of the EA19 average.

In the case of the **labour market component**, which gives the number of hours worked per working-age person, there is the opposite situation. In 2016, the relative level of the labour market component exceeded the average of the EA19 countries in all states except Slovakia; in Estonia, Lithuania, Latvia, the Czech Republic and Poland the gap exceeded 20 pp. In 2008–2016, the absolute level of the labour force component dropped in Greece, Latvia, Portugal, Estonia, Slovenia and Hungary, with Greece recording a decline by 14% in the reported years as a result of a 19% drop in hours worked.

The share of the working-age population, captured by the **demographic component**, reached its peak in most monitored countries during the first decade of the 21st century and is now decreasing due to population ageing. In 2008–2016, the sharpest decrease, of 5.1 pp, was recorded in the Czech Republic. Compared to the EA19 average, however, the demographic component is still higher in all monitored countries except Latvia and Poland; in Slovakia it exceeded the EA19 average by 9 pp in 2016.

<sup>6</sup> GDP per capita can be written as follows:

$$\begin{aligned} \text{GDP per capita} &= \frac{\text{GDP}}{\text{number of inhabit.}} = \\ &= \frac{\text{GDP}}{\text{no. of hours worked}} * \frac{\text{no. of hours worked}}{\text{population aged 15–64}} * \frac{\text{population aged 15–64}}{\text{no. of inhabit.}} = \\ &= \text{labour productivity} * \text{labour market component} * \text{demographic component} \end{aligned}$$

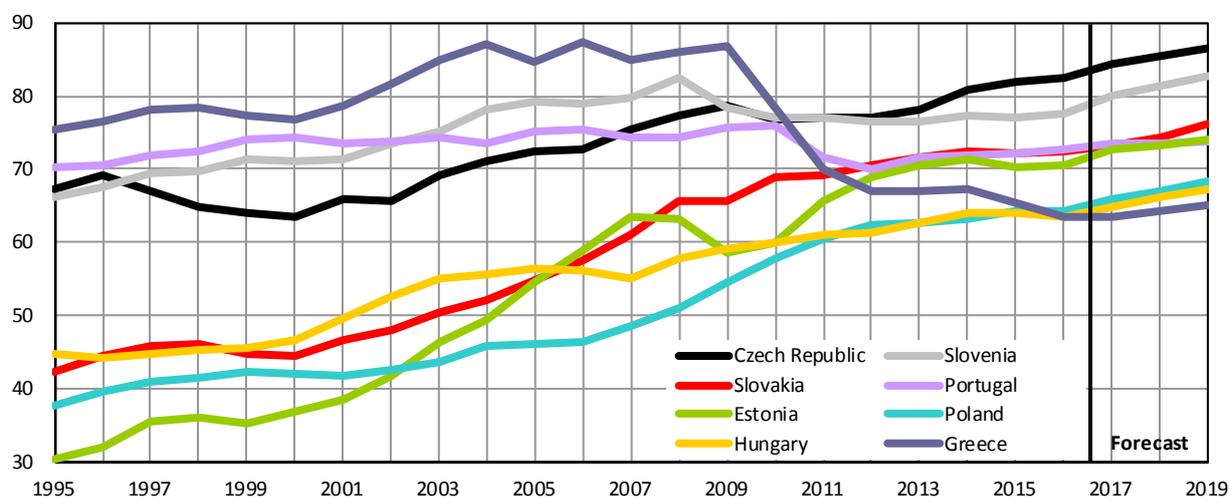
**Table 3.5.1: GDP per Capita – Using Current Purchasing Power Parities**

		2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
									<i>Estimate</i>	<i>Forecast</i>	<i>Forecast</i>
<b>Spain</b>	PPS	<b>24 400</b>	<b>24 200</b>	<b>24 200</b>	<b>24 000</b>	<b>24 900</b>	<b>26 300</b>	<b>26 700</b>	<b>27 800</b>	<b>29 000</b>	<b>30 000</b>
	EA19=100	89	86	85	84	84	85	86	87	87	88
<b>Czech Republic</b>	PPS	<b>21 100</b>	<b>21 700</b>	<b>22 000</b>	<b>22 400</b>	<b>23 800</b>	<b>25 300</b>	<b>25 600</b>	<b>26 900</b>	<b>28 300</b>	<b>29 600</b>
	EA19=100	77	77	77	78	81	82	82	84	85	87
<b>Slovenia</b>	PPS	<b>21 200</b>	<b>21 700</b>	<b>21 800</b>	<b>21 900</b>	<b>22 700</b>	<b>23 800</b>	<b>24 100</b>	<b>25 600</b>	<b>26 900</b>	<b>28 200</b>
	EA19=100	77	77	77	76	77	77	78	80	81	83
<b>Lithuania</b>	PPS	<b>15 400</b>	<b>17 200</b>	<b>18 600</b>	<b>19 600</b>	<b>20 800</b>	<b>21 700</b>	<b>22 000</b>	<b>23 500</b>	<b>24 800</b>	<b>26 200</b>
	EA19=100	56	61	65	68	70	70	71	73	75	77
<b>Slovakia</b>	PPS	<b>19 000</b>	<b>19 500</b>	<b>20 100</b>	<b>20 500</b>	<b>21 300</b>	<b>22 300</b>	<b>22 400</b>	<b>23 400</b>	<b>24 600</b>	<b>26 000</b>
	EA19=100	69	69	71	72	72	72	72	73	74	76
<b>Portugal</b>	PPS	<b>20 900</b>	<b>20 200</b>	<b>20 000</b>	<b>20 500</b>	<b>21 200</b>	<b>22 300</b>	<b>22 600</b>	<b>23 500</b>	<b>24 400</b>	<b>25 200</b>
	EA19=100	76	72	70	72	72	72	73	73	74	74
<b>Estonia</b>	PPS	<b>16 500</b>	<b>18 500</b>	<b>19 600</b>	<b>20 200</b>	<b>21 000</b>	<b>21 700</b>	<b>21 900</b>	<b>23 200</b>	<b>24 200</b>	<b>25 300</b>
	EA19=100	60	66	69	70	71	70	71	73	73	74
<b>Poland</b>	PPS	<b>15 900</b>	<b>17 000</b>	<b>17 800</b>	<b>17 900</b>	<b>18 600</b>	<b>19 800</b>	<b>19 900</b>	<b>21 100</b>	<b>22 200</b>	<b>23 400</b>
	EA19=100	58	60	62	63	63	64	64	66	67	68
<b>Hungary</b>	PPS	<b>16 500</b>	<b>17 200</b>	<b>17 500</b>	<b>18 000</b>	<b>18 800</b>	<b>19 700</b>	<b>19 700</b>	<b>20 700</b>	<b>21 900</b>	<b>23 000</b>
	EA19=100	60	61	61	63	64	64	63	65	66	67
<b>Latvia</b>	PPS	<b>13 400</b>	<b>14 900</b>	<b>16 100</b>	<b>16 700</b>	<b>17 500</b>	<b>18 500</b>	<b>18 800</b>	<b>20 100</b>	<b>21 300</b>	<b>22 600</b>
	EA19=100	49	53	56	58	60	60	61	63	64	66
<b>Greece</b>	PPS	<b>21 500</b>	<b>19 700</b>	<b>19 100</b>	<b>19 200</b>	<b>19 800</b>	<b>20 200</b>	<b>19 700</b>	<b>20 300</b>	<b>21 300</b>	<b>22 300</b>
	EA19=100	78	70	67	67	67	65	64	64	64	65
<b>Croatia</b>	PPS	<b>15 100</b>	<b>15 600</b>	<b>16 000</b>	<b>16 000</b>	<b>16 300</b>	<b>17 200</b>	<b>17 500</b>	<b>18 300</b>	<b>19 200</b>	<b>20 100</b>
	EA19=100	55	55	56	56	55	56	56	57	58	59

Source: AMECO, CZSO, Eurostat. Calculations of the MoF.

**Graph 3.5.1: GDP per Capita – Using Current Purchasing Power Parities**

EA19=100



Source: AMECO, CZSO, Eurostat. Calculations of the MoF.

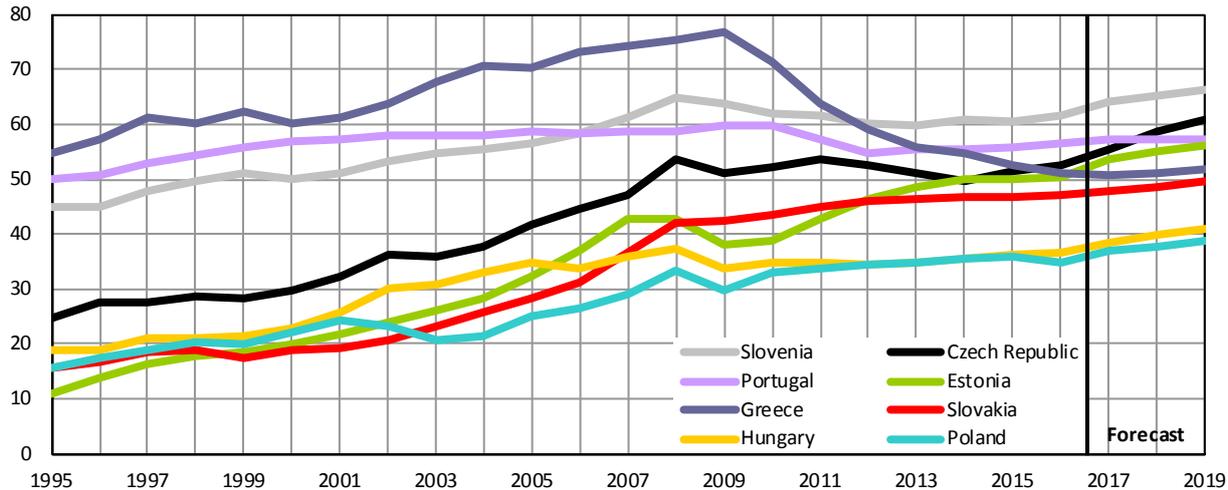
**Table 3.5.2: GDP per Capita – Using Current Exchange Rates**

		2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
									<i>Estimate</i>	<i>Forecast</i>	<i>Forecast</i>
<b>Spain</b>	<i>EUR</i>	<b>23 200</b>	<b>22 900</b>	<b>22 200</b>	<b>22 000</b>	<b>22 300</b>	<b>23 300</b>	<b>24 100</b>	<b>25 000</b>	<b>26 100</b>	<b>27 000</b>
	<i>EA19=100</i>	81	78	76	75	74	75	76	76	77	77
	<i>Comparative price level EA19=100</i>	<b>92</b>	<b>92</b>	<b>90</b>	<b>89</b>	<b>88</b>	<b>88</b>	<b>88</b>	<b>88</b>	<b>88</b>	<b>88</b>
<b>Slovenia</b>	<i>EUR</i>	<b>17 700</b>	<b>18 000</b>	<b>17 500</b>	<b>17 600</b>	<b>18 200</b>	<b>18 800</b>	<b>19 600</b>	<b>21 000</b>	<b>22 100</b>	<b>23 200</b>
	<i>EA19=100</i>	62	62	60	60	61	61	62	64	65	66
	<i>Comparative price level EA19=100</i>	<b>80</b>	<b>80</b>	<b>78</b>	<b>78</b>	<b>79</b>	<b>79</b>	<b>79</b>	<b>80</b>	<b>80</b>	<b>80</b>
<b>Czech Republic</b>	<i>EUR</i>	<b>14 900</b>	<b>15 600</b>	<b>15 400</b>	<b>15 000</b>	<b>14 900</b>	<b>16 000</b>	<b>16 700</b>	<b>18 100</b>	<b>19 900</b>	<b>21 300</b>
	<i>EA19=100</i>	52	54	53	51	50	52	53	55	59	61
	<i>Comparative price level EA19=100</i>	<b>68</b>	<b>70</b>	<b>68</b>	<b>65</b>	<b>61</b>	<b>63</b>	<b>64</b>	<b>66</b>	<b>69</b>	<b>70</b>
<b>Portugal</b>	<i>EUR</i>	<b>17 000</b>	<b>16 700</b>	<b>16 000</b>	<b>16 300</b>	<b>16 600</b>	<b>17 400</b>	<b>18 000</b>	<b>18 700</b>	<b>19 400</b>	<b>20 100</b>
	<i>EA19=100</i>	60	57	55	55	55	56	57	57	57	57
	<i>Comparative price level EA19=100</i>	<b>79</b>	<b>80</b>	<b>78</b>	<b>77</b>	<b>77</b>	<b>78</b>	<b>78</b>	<b>78</b>	<b>78</b>	<b>78</b>
<b>Estonia</b>	<i>EUR</i>	<b>11 000</b>	<b>12 500</b>	<b>13 500</b>	<b>14 300</b>	<b>15 000</b>	<b>15 500</b>	<b>16 000</b>	<b>17 500</b>	<b>18 600</b>	<b>19 700</b>
	<i>EA19=100</i>	39	43	46	49	50	50	51	53	55	56
	<i>Comparative price level EA19=100</i>	<b>65</b>	<b>66</b>	<b>67</b>	<b>69</b>	<b>70</b>	<b>71</b>	<b>72</b>	<b>74</b>	<b>75</b>	<b>76</b>
<b>Greece</b>	<i>EUR</i>	<b>20 300</b>	<b>18 600</b>	<b>17 300</b>	<b>16 500</b>	<b>16 400</b>	<b>16 300</b>	<b>16 200</b>	<b>16 600</b>	<b>17 300</b>	<b>18 100</b>
	<i>EA19=100</i>	71	64	59	56	55	53	51	51	51	52
	<i>Comparative price level EA19=100</i>	<b>91</b>	<b>91</b>	<b>88</b>	<b>84</b>	<b>81</b>	<b>80</b>	<b>80</b>	<b>80</b>	<b>80</b>	<b>80</b>
<b>Slovakia</b>	<i>EUR</i>	<b>12 400</b>	<b>13 100</b>	<b>13 400</b>	<b>13 700</b>	<b>14 000</b>	<b>14 600</b>	<b>14 900</b>	<b>15 600</b>	<b>16 400</b>	<b>17 400</b>
	<i>EA19=100</i>	44	45	46	47	47	47	47	48	49	50
	<i>Comparative price level EA19=100</i>	<b>63</b>	<b>65</b>	<b>65</b>	<b>65</b>						
<b>Lithuania</b>	<i>EUR</i>	<b>9 000</b>	<b>10 300</b>	<b>11 200</b>	<b>11 800</b>	<b>12 500</b>	<b>12 900</b>	<b>13 500</b>	<b>14 800</b>	<b>16 100</b>	<b>17 200</b>
	<i>EA19=100</i>	32	35	38	40	42	42	43	45	47	49
	<i>Comparative price level EA19=100</i>	<b>57</b>	<b>58</b>	<b>58</b>	<b>59</b>	<b>59</b>	<b>59</b>	<b>60</b>	<b>62</b>	<b>63</b>	<b>64</b>
<b>Latvia</b>	<i>EUR</i>	<b>8 500</b>	<b>9 800</b>	<b>10 800</b>	<b>11 300</b>	<b>11 800</b>	<b>12 300</b>	<b>12 700</b>	<b>13 900</b>	<b>15 000</b>	<b>16 100</b>
	<i>EA19=100</i>	30	34	37	39	39	40	40	42	44	46
	<i>Comparative price level EA19=100</i>	<b>61</b>	<b>64</b>	<b>66</b>	<b>66</b>	<b>66</b>	<b>66</b>	<b>66</b>	<b>67</b>	<b>68</b>	<b>70</b>
<b>Hungary</b>	<i>EUR</i>	<b>9 900</b>	<b>10 200</b>	<b>10 000</b>	<b>10 300</b>	<b>10 700</b>	<b>11 200</b>	<b>11 600</b>	<b>12 600</b>	<b>13 500</b>	<b>14 400</b>
	<i>EA19=100</i>	35	35	34	35	36	36	37	39	40	41
	<i>Comparative price level EA19=100</i>	<b>58</b>	<b>57</b>	<b>56</b>	<b>56</b>	<b>56</b>	<b>57</b>	<b>58</b>	<b>60</b>	<b>60</b>	<b>61</b>
<b>Poland</b>	<i>EUR</i>	<b>9 400</b>	<b>9 900</b>	<b>10 100</b>	<b>10 300</b>	<b>10 700</b>	<b>11 200</b>	<b>11 100</b>	<b>12 100</b>	<b>12 800</b>	<b>13 600</b>
	<i>EA19=100</i>	33	34	35	35	36	36	35	37	38	39
	<i>Comparative price level EA19=100</i>	<b>57</b>	<b>56</b>	<b>55</b>	<b>56</b>	<b>56</b>	<b>56</b>	<b>54</b>	<b>56</b>	<b>56</b>	<b>57</b>
<b>Croatia</b>	<i>EUR</i>	<b>10 500</b>	<b>10 500</b>	<b>10 300</b>	<b>10 300</b>	<b>10 200</b>	<b>10 600</b>	<b>11 100</b>	<b>11 800</b>	<b>12 300</b>	<b>13 000</b>
	<i>EA19=100</i>	37	36	35	35	34	34	35	36	36	37
	<i>Comparative price level EA19=100</i>	<b>67</b>	<b>65</b>	<b>63</b>	<b>62</b>	<b>62</b>	<b>61</b>	<b>62</b>	<b>63</b>	<b>63</b>	<b>63</b>

Source: AMECO, CZSO, Eurostat. Calculations of the MoF.

**Graph 3.5.2: GDP per Capita – Using Current Exchange Rates**

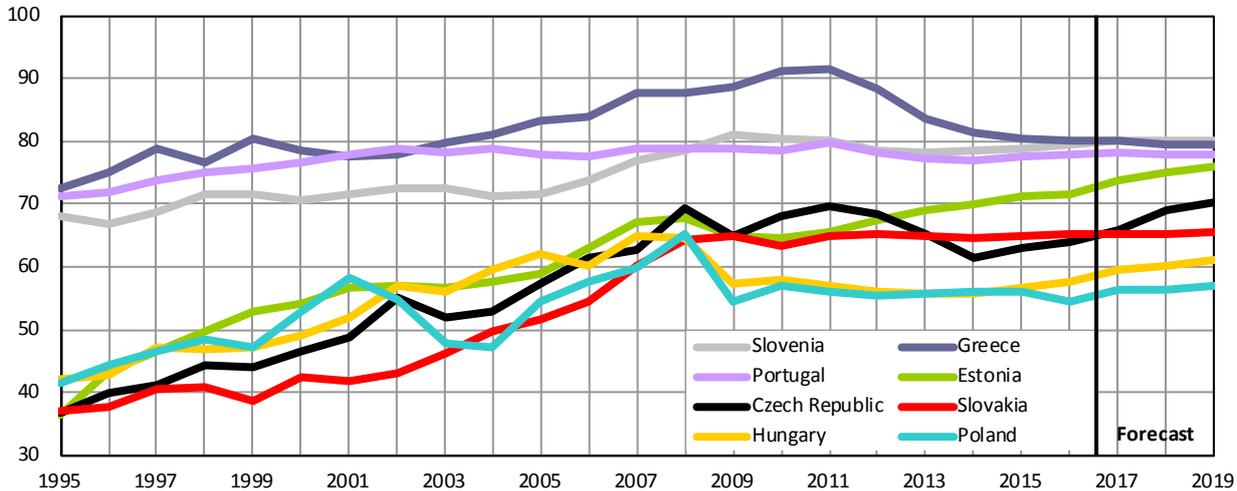
EA19=100



Source: AMECO, CZSO, Eurostat. Calculations of the MoF.

**Graph 3.5.3: Comparative Price Level of GDP per Capita**

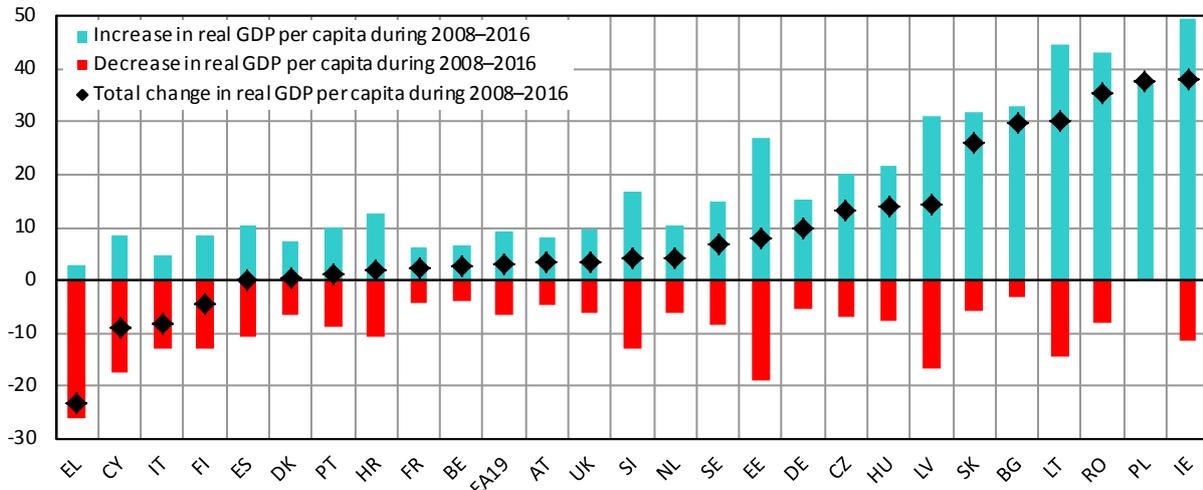
EA19=100



Source: AMECO, CZSO, Eurostat. Calculations of the MoF.

**Graph 3.5.4: Change in Real GDP per Capita during 2008–2016**

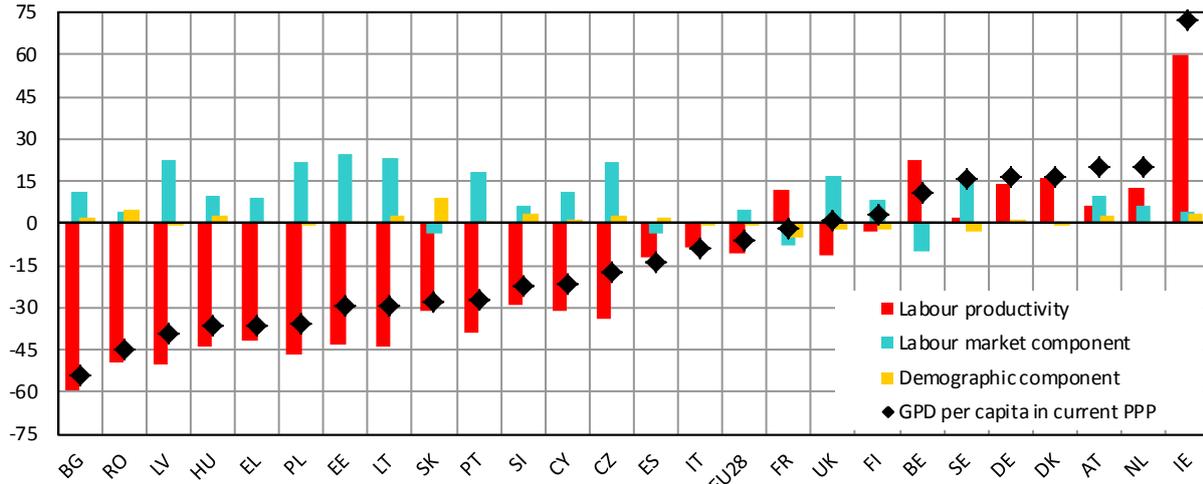
growth in %



Source: Eurostat. Calculations of the MoF.

**Graph 3.5.5: Current PPP Adjusted GDP per Capita Level Relative to the EA19 Average in 2016**

in percentage points

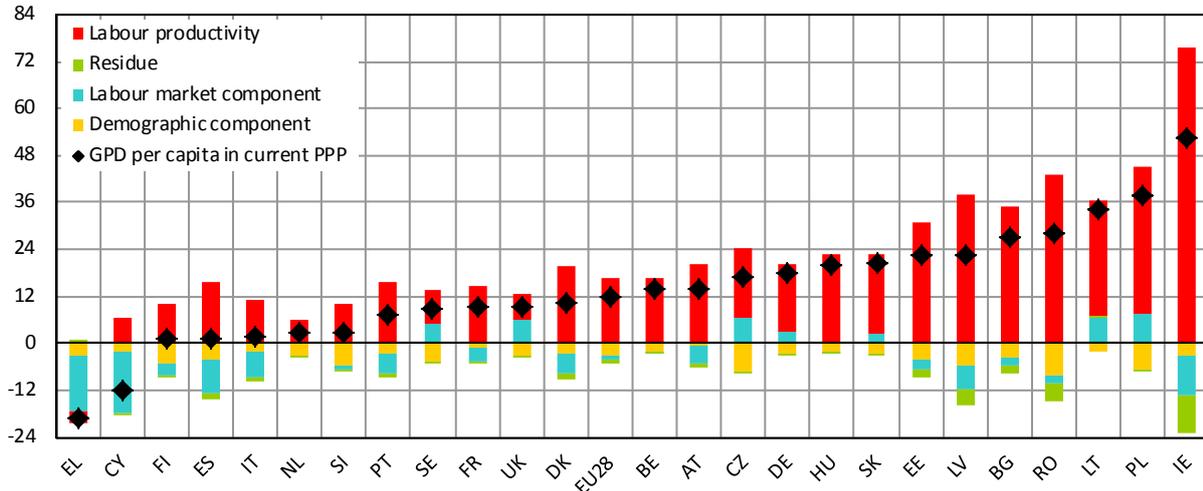


Note: The labour market component is defined as the ratio of total hours worked to working-age (15–64) population, the demographic component is the ratio of the working-age to total population.

Source: Eurostat. Calculations of the MoF.

**Graph 3.5.6: Change in Current PPP Adjusted GDP per Capita during 2008–2016**

growth in %



Source: Eurostat. Calculations of the MoF.

## 4 Monitoring of Other Institutions' Forecasts

The Ministry of Finance of the Czech Republic monitors macroeconomic forecasts of other institutions engaged in forecasting the Czech economy. Publicly available forecasts of 12 institutions are monitored. Out of these, 7 institutions are domestic (CNB, Ministry of Labour and Social Affairs, domestic banks and investment companies) and the others are foreign (European Commission, Organisation for Economic Co-operation and Development, IMF, etc.) The forecasts are summarised in Table 4.1.

**Table 4.1: Summary of the Monitored Forecasts**

		March 2018			April 2018
		min.	max.	average	MoF forecast
Gross domestic product (2018)	growth in %, const.pr.	2.6	3.8	3.4	3.6
Gross domestic product (2019)	growth in %, const.pr.	2.5	3.2	2.9	3.3
Average inflation rate (2018)	%	1.8	2.6	2.3	2.1
Average inflation rate (2019)	%	1.9	2.3	2.1	1.9
Average monthly wage (2018)	growth in %	6.2	7.8	7.3	7.3
Average monthly wage (2019)	growth in %	3.5	6.2	5.1	6.3
Current account / GDP (2018)	%	0.1	1.1	0.7	0.4
Current account / GDP (2019)	%	0.4	1.7	0.9	0.2

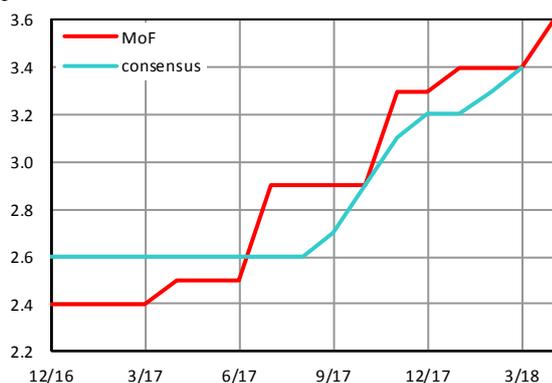
Source: Forecasts of individual institutions. Calculations of the MoF.

According to the average of monitored institutions' estimates, real GDP growth should reach 3.4% in 2018 and then slow down slightly to 2.9% in 2019. The average inflation rate should hover close to the CNB's inflation target in 2018 and 2019, and reach 2.3% and 2.1%, respectively. The average wage growth should slow down sharply from dynamic 7.3% in 2018 to only 5.1% in 2019. The current account of the balance payments surplus should oscillate around 0.8% of GDP in 2018 and 2019.

In the case of the estimate of real GDP developments and the average inflation rate, the forecast of the MoF is in line with the average of the monitored institutions' forecasts. As regards the average wage developments, the MoF expects a more dynamic growth in 2019, of 6.3%. According to the MoF, the surplus on the current account of the balance payments should be slightly lower in comparison with the average of the monitored institutions' forecasts.

**Graph 4.1: Forecasts for Real GDP Growth in 2018**

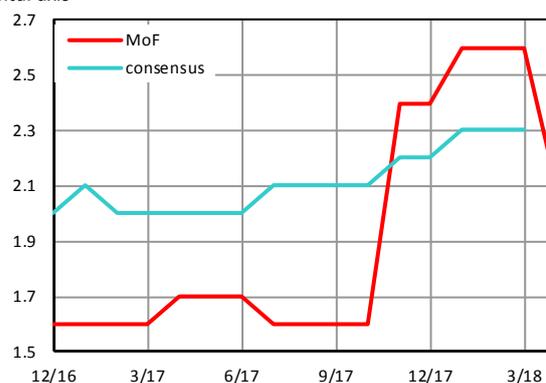
in %; the month, in which the monitoring was conducted on the horizontal axis



Source: Forecasts of individual institutions. Calculations of the MoF.

**Graph 4.2: Forecasts for Average Inflation Rate in 2018**

in %; the month, in which the monitoring was conducted on the horizontal axis



Source: Forecasts of individual institutions. Calculations of the MoF.

## 5 Looking back at the Year 2017

The macroeconomic framework of the state budget for 2017 was based on the July 2016 Macroeconomic Forecast.

The text below compares the macroeconomic framework of the state budget with the data for 2017 published by 3 April 2018. For most indicators, however, the data cannot be considered definitive as they will be further revised.

In retrospect, it can be said that the state budget was based on a very conservative macroeconomic framework. Economic growth in 2017 as well as the development of all indicators relevant for the budget performance of the general government sector was substantially more favourable than the macroeconomic framework.

**Table 5.1: Macroeconomic Framework of the 2017 State Budget – Comparison with Actual Data**

	2017 State Budget (July 2016)				Outcome (April 2018)				Difference (outcome - forecast)				
	2014	2015	2016	2017	2014	2015	2016	2017	2014	2015	2016	2017	
	Forecast				Prelim.								
Gross domestic product	bill. CZK	4 314	4 555	4 681	4 846	4 314	4 596	4 773	5 055	0	41	92	209
Gross domestic product	growth in %, curr.pr.	5,3	5,6	2,8	3,5	5,3	6,5	3,9	5,9	0,0	0,9	1,1	2,4
Consumption of households	growth in %, curr.pr.	2,4	3,2	3,3	3,9	2,4	3,8	4,2	6,5	0,0	0,6	0,9	2,6
Gross domestic product	growth in %, const.pr.	2,7	4,5	2,2	2,4	2,7	5,3	2,6	4,4	0,0	0,8	0,4	2,0
Consumption of households	growth in %, const.pr.	1,8	3,0	3,1	2,7	1,8	3,7	3,6	4,0	0,0	0,7	0,5	1,3
Consumption of government	growth in %, const.pr.	1,1	2,0	2,2	1,6	1,1	1,9	2,0	1,5	0,0	-0,1	-0,2	-0,1
Gross fixed capital formation	growth in %, const.pr.	3,9	9,0	-0,6	2,8	3,9	10,2	-2,3	5,4	0,0	1,2	-1,7	2,6
Contr. of net exports to GDP growth	p.p., const.pr.	-0,5	0,1	0,7	0,2	-0,5	-0,2	1,2	1,0	0,0	-0,3	0,5	0,8
GDP deflator	growth in %	2,5	1,0	0,6	1,1	2,5	1,2	1,2	1,4	0,0	0,2	0,6	0,3
Average inflation rate	%	0,4	0,3	0,5	1,2	0,4	0,3	0,7	2,5	-	-	0,2	1,3
Employment (LFS)	growth in %	0,8	1,4	1,6	0,1	0,8	1,4	1,9	1,6	-	-	0,3	1,5
Unemployment rate (LFS)	average in %	6,1	5,1	4,1	4,0	6,1	5,1	4,0	2,9	-	-	-0,1	-1,1
Share of unemployed	average in %	7,7	6,6	5,6	5,4	7,7	6,6	5,6	4,3	-	-	0,0	-1,1
Wage bill (domestic concept)	growth in %, curr.pr.	3,6	4,4	5,3	4,9	3,6	4,8	5,8	8,3	0,0	0,4	0,5	3,4
Current account balance	% of GDP	0,2	0,9	1,5	1,2	0,2	0,2	1,1	0,5	0,0	-0,7	-0,4	-0,7
<u>Assumptions:</u>													
Exchange rate CZK/EUR		27,5	27,3	27,0	26,9	27,5	27,3	27,0	26,3	-	-	0,0	-0,6
Long-term interest rates	% p.a.	1,6	0,6	0,6	0,8	1,6	0,6	0,4	1,0	-	-	-0,2	0,2
Crude oil Brent	USD/barrel	99	52	44	50	99	52	44	54	-	-	0	4
GDP of the euro area (EA12)	growth in %, const.pr.	0,9	1,6	1,5	1,2	1,3	2,0	1,8	2,3	0,4	0,4	0,3	1,1

Source: CNB, CZSO, Eurostat, MoF, U. S. Energy Information Administration. Calculations of the MoF.

At the time of preparation of the macroeconomic framework of the state budget, the economy was in a period of a temporary slowdown in economic dynamics after a record growth in 2015, when, however, the economy was largely stimulated by the end of the previous financial perspective for EU projects.

According to the then available data, real GDP increased by 0.4% QoQ in the first quarter of 2016, and by 2.7% in a YoY comparison. Consumption of households grew at a similar pace (2.6%), while gross fixed capital formation stagnated in YoY terms (specifically, declined by 0.1%).

The subsequent revision of the quarterly national accounts showed, however, that the then valid estimates of economic dynamics were largely underestimated. According to the currently valid data, the QoQ real GDP growth in the first quarter of 2016 remained essentially unchanged at 0.3%, but the YoY growth was revised up to

3.2%. Similarly, the household consumption growth was increased to 3.8%, and gross fixed capital formation growth to 0.4%. The intensity of the slowdown in growth at the beginning of 2016 was thus considerably lower than we thought when compiling the macroeconomic framework of the state budget.

However, the assumptions of the framework were more or less fulfilled. The CNB discontinued its exchange rate commitment at the beginning of the second quarter of 2017, and the exchange rate of the koruna started appreciating. A gradual increase of long-term interest rates was also expected. The crude oil price also basically copied the expected trajectory.

On the contrary, the economic growth of the main trading partners was a very positive surprise. That was reflected in the contribution of foreign trade in goods and services to GDP growth, which, despite a higher than

predicted growth in domestic demand (including import-intensive investments), reached 1.0 pp instead of the expected 0.2 pp.

The average inflation rate was significantly higher in 2017, reaching 2.5% versus the forecast of 1.2%. The main cause was an unexpected rise in food prices at the end of 2016 and early 2017.

The labour market situation surpassed all expectations. Contrary to the forecast, dynamic growth in employment continued also in 2017, resulting in an increase of 1.6%. The unemployment rate (LFS), which had been the lowest in the EU since the beginning of 2016, averaged 2.9% in 2017 versus a forecast of 4.0%. The share of unemployed persons (Ministry of Labour and Social Affairs) dropped to 4.3%, which was 1.1 pp less in comparison with the macroeconomic framework.

The strong employment growth, further significant increase in the minimum wage and in salaries in the general government sector and the increasing shortage of employees with suitable qualification contributed to the fact that the wage bill increased by 8.3% versus 4.9% envisaged in the macroeconomic framework of the state budget for 2017.

Significantly more favourable developments of employment, better consumer confidence and, in particular, faster than expected wage growth accelerated the real household consumption growth to 4.0% instead of the expected 2.7%. The higher inflation then led to the fact that the nominal household consumption growth of 6.5% significantly exceeded the estimate of the macroeconomic framework, which was 3.9%.

The stronger than expected growth in economies of the main trading partners and the tighter labour market situation supported investment growth. Investment in machinery and equipment (including transport equipment) and in information and communication technologies were components that most contributed to the gross fixed capital formation increase. The consequent 5.4% increase in investment thus exceeded the forecast by 2.6 pp.

As a result, the 4.4% real GDP growth significantly – by full 2 pp – exceeded the forecast; in the case of nominal growth, the bias was even bigger.

The surprisingly positive macroeconomic development in 2017 can be considered a synergic result of many essentially random favourable circumstances. Therefore, it is unlikely to recur in the near future.

