

## Risks to the Forecast

The up-to-date quarterly national accounts data for Q3 2013 showed that **economic recovery** following the recession, which ended in Q1 2013, is only **very slow**. Moreover, the development of individual components of real GDP use was very volatile. The fact that real gross value added continued to decrease QoQ is a cause for great concern. No considerable increase in gross value added was recorded in any one of the 11 sectors of the NACE classification.

The sustainability and intensity of the recovery are still uncertain. Therefore, the central scenario of the Macroeconomic Forecast is **rather more conservative** in comparison with other forecasts for the Czech economy (see Chapter D).

The scenario envisages that the Czech Republic's economy is gradually entering a period of slowly growing economic output. This should be reflected in a YoY increase in real GDP of 1.4% in 2014 and of 2.0% in 2015. In 2014, both domestic and foreign demand should equally contribute to this result, while in 2015 the weight of domestic expenditures should increase.

**The risks of the scenario are considered to be more or less balanced.**

As far as the **external environment** is concerned, one can emphasise a **positive risk** that the global economy may grow more quickly than the central scenario assumes.

Even though the euro zone will probably remain the slowest growing region on a global scale, the chances are that the **recovery of export-oriented economies of Germany** and some other main trading partners of the Czech Republic may be **stronger**. This is what the confidence indicators in these countries might indicate (see Chapter A.1).

However, the still unresolved crisis in the euro zone remains a **negative risk**. Macroeconomic indicators and development on the government bonds markets at least suggest that from the short-term perspective the situation has calmed down and any major upheavals are not very likely. In the troubled euro zone countries, however, the government sector debt is still very high, the situation regarding the quality of financial sector assets unclear and the social situation, which can be judged especially by the high unemployment rate, gloomy. In the medium-term, it is thus not possible to

completely neglect the risk of a possible further escalation of the crisis in the euro zone (see Chapter A.1).

**The biggest negative risk within the Czech economy** is the fact that it is "frozen" after a 5-year period of alternating recessions and stagnation. In Q3 2013, real gross fixed capital formation was 25.1% lower than at the top of the investment cycle in Q1 2008. Seasonally adjusted number of registered unemployed persons increased from 319 thousand in August 2008 to 578 thousand in December 2013.

On the other hand, the results of business cycle indicators (see Chapter B.2) suggest **considerable improvement** in most of the examined segments (except for construction), which is also partially confirmed by the current data on industrial production and retail sales. However, it remains an open question as to whether and how quickly improvements in business cycle indicators will be reflected in the individual components of domestic demand.

The recent **CNB decision to use the exchange rate as an additional monetary policy instrument** (see Chapter A.3) has considerably changed the setting of economic policy, whereby the uncertainty of forecasts has become more pronounced. The central scenario includes the probable macroeconomic impacts of foreign exchange interventions, but completely arbitrary assumptions had to be made for a number of aspects (e.g. regarding the date when the CNB will stop using the interventions). We perceive the possible stronger response in exports to the weakening of the exchange rate as a positive risk. However, a negative risk is the potential impact of higher than originally expected inflation on household consumption (even if the foreign trade balance improves due to lower consumption).

Even in this Macroeconomic Forecast, the situation and developments on the domestic political scene are an area of uncertainty. A coalition government with clear majority of mandates has been appointed on the basis of the results of early elections to the Chamber of Deputies of the Parliament of the Czech Republic, but its policy statement has not been published yet. This prevents the government's planned economic policy from being assessed in detail.