Summary of the Forecast

Real GDP, which showed a surprisingly marked QoQ decline of 1.3% in Q1 2013, increased by 0.6% QoQ in Q2 2013. The economy technically emerged from the 18-month recession; however, GDP was 1.3% lower than in Q2 2012. Despite the expected economic recovery, economic output for the whole year should decrease by 1.0%, in particular due to a decline in gross capital formation. In 2014, however, with a positive contribution from all components except for fixed investment, GDP could increase by 1.3%.

Consumer prices should grow at a sluggish pace. We expect the average inflation rate to reach 1.4% in 2013 and 0.7% in 2014. Inflation in 2014 will be very low in particular thanks to a decline in electricity prices.

Employment, the YoY growth of which was accelerating throughout the whole of the last year despite the recession, could increase by 1.2% this year. This somewhat paradoxical development was caused by a rise in the number of part-time jobs and a decline in the ratio of total hours worked to employment. For 2014, employment growth of 0.4% is estimated. The unemployment rate (LFS) should be slowly rising from the last year's 7.0%. It could reach 7.1% in 2013 and 7.3% in 2014. Growth in the wage bill, which should reach 0.8% in 2013, could accelerate to 2.5% in 2014. Therefore, the total wage bill growth rate is expected to exceed the dynamics of nominal GDP in both years.

According to the MoF's end-September notifications, the government sector deficit should reach 2.9% of GDP in 2013, which is also the target value for 2014. In addition to the rules of the Stability and Growth Pact, any room for the stabilizing role of fiscal policy is also restricted by the persisting structural deficits of the government sector.

The current account deficit should not exceed 2% of GDP, which is a sustainable level fully consistent with the external macroeconomic balance.

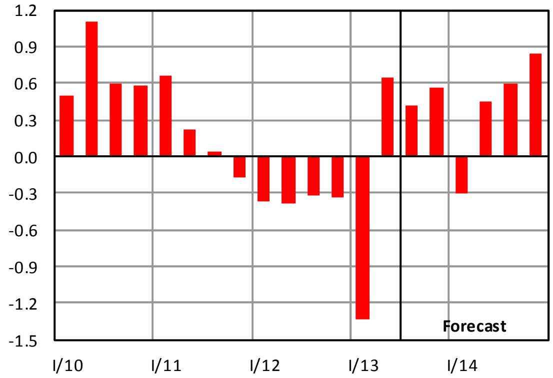
Despite an uncertain outlook for the external environment and the still relatively low confidence of domestic agents in future economic development, we evaluate the forecast risks as balanced.

Table: **Main Macroeconomic Indicators**

		2010	2011	2012	2013	2014	2012	2013	2014
					Current forecast			*Previous forecast*	
Gross domestic product	*growth in %, const.pr.*	**2.5**	**1.8**	**-1.0**	**-1.0**	**1.3**	-1.2	-1.5	0.8
Consumption of households	*growth in %, const.pr.*	**0.9**	**0.5**	**-2.1**	**0.2**	**0.9**	-2.7	-0.8	0.4
Consumption of government	*growth in %, const.pr.*	**0.2**	**-2.7**	**-1.9**	**0.8**	**0.2**	-1.2	0.5	-0.9
Gross fixed capital formation	*growth in %, const.pr.*	**1.0**	**0.4**	**-4.5**	**-4.8**	**-0.8**	-2.7	-4.3	-0.6
Cont. of foreign trade to GDP growth	*p.p., const.pr.*	**0.6**	**1.9**	**1.7**	**0.6**	**0.6**	1.4	0.2	0.5
GDP deflator	*growth in %*	**-1.6**	**-0.9**	**1.6**	**1.2**	**0.5**	1.4	0.6	0.9
Average inflation rate	*%*	**1.5**	**1.9**	**3.3**	**1.4**	**0.7**	3.3	1.6	1.4
Employment *(LFS)*	*growth in %*	**-1.0**	**0.4**	**0.4**	**1.2**	**0.4**	0.4	0.5	-0.2
Unemployment rate *(LFS)*	*average in %*	**7.3**	**6.7**	**7.0**	**7.1**	**7.3**	7.0	7.5	7.6
Wage bill *(domestic concept)*	*growth in %, curr.pr.*	**0.8**	**2.2**	**1.8**	**0.8**	**2.5**	1.5	0.7	2.1
Current account / GDP	*%*	**-3.9**	**-2.7**	**-2.4**	**-1.7**	**-1.4**	-2.5	-2.3	-2.4
Assumptions:									
Exchange rate CZK/EUR		**25.3**	**24.6**	**25.1**	**25.8**	**25.8**	25.1	25.8	25.8
Long-term interest rates	*% p.a.*	**3.7**	**3.7**	**2.8**	**2.1**	**2.4**	2.8	2.0	2.2
Crude oil Brent	*USD/barrel*	**80**	**111**	**112**	**108**	**103**	112	106	101
GDP in Eurozone (EA-12)	*growth in %, const.pr.*	**1.9**	**1.6**	**-0.6**	**-0.3**	**1.0**	-0.6	-0.5	1.0

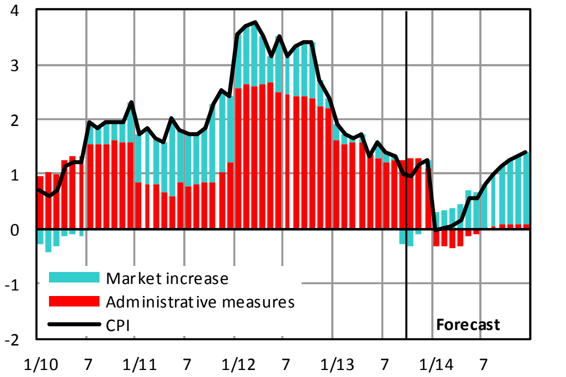
Gradual economic recovery expected

real GDP, QoQ growth in %, seasonally adjusted



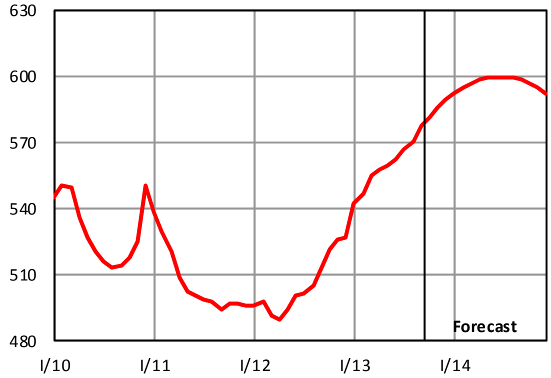
Sluggish growth of consumer prices

decomposition of YoY growth in consumer prices, percentage points



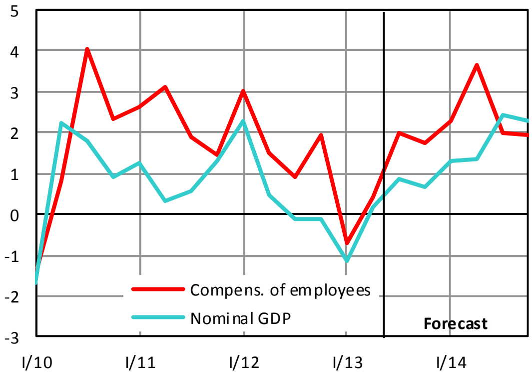
Unemployment culminating in mid-2014

registered unemployment, in thousands of persons, seasonally adjusted



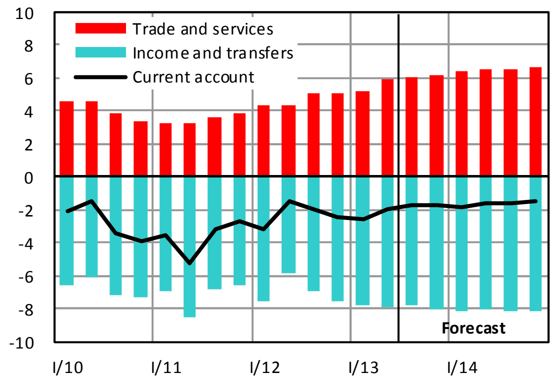
Rising share of compensation of employees on GDP

growth in %



Low current account deficit

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



Government sector deficit below 3% of GDP in 2013

general government balance, in % of GDP