

Risks to the Forecast

The central scenario of this Macroeconomic Forecast envisages that in YoY terms GDP will stagnate in 2013. **Nevertheless the risks of this forecast are slightly tilted to the downside.**

As far as the assumptions of the central scenario on the external environment are concerned, **the euro zone's prospects** for both this and the next year have **deteriorated further** (similarly to the Winter 2013 European Economic Forecast of the EC).

In Q4 2012, there was a surprisingly deep decline in the euro zone's economic activity, even in the "core" countries. The leading indicators provide mixed signals for the next 6 months to come.

The most important **economic risk** related to the external environment is, in our view, the threat of the recession being experienced in the south of the euro zone spilling over to the countries of the Czech Republic's main trading partners, especially to Germany. Should this risk materialise, it would result in an even more significant decrease in the contribution of foreign trade to the GDP change than expected in the Forecast.

In problematic countries, the economic situation is further deteriorating. Greece is in deep depression. According to the EC forecast, Greek GDP will have cumulatively declined by 23.6% this year, compared with 2007. Such an economic slump (already comparable to the Great Depression of 1929–1933 when e.g. US economic performance decreased by 28.5%, according to the OECD data) has not yet occurred in the post-war history of developed countries, with the exception of Latvia (whose GDP declined cumulatively by nearly a quarter between Q1 2008 and Q3 2009).

Compared with Q3 2010, the total economic decline in Portugal has already reached 7.0%. The Cypriot economy has so far shrunk by 4.2%, compared with Q2 2011. However, implementation of the bailout programme (a combination of fiscal restriction,

structural reforms and restructuring and significant downsizing of the banking sector) is likely to plunge the country into depression. Smaller in extent, though also significant, is the depth of the recession in Italy (cumulative GDP decline of 3.7%, compared with Q2 2011) and in Spain (cumulative decline of 2.5%). Sharp downturn in problematic economies, accompanied by rising unemployment rate and negligible prospects for the economic situation to improve soon, accelerates **political and social risks**. These are reflected e.g. in stalemate results of the Italian elections.

In comparison with the second half of 2012, we consider the short-term **risks related to the debt crisis in the euro zone** to be less serious. The situation on the financial markets has gradually settled down, contributed for instance by the possibility of ECB interventions on the secondary market for government bonds under the OMTs programme as well as launching of the ESM mechanism. However, as the course of negotiations on the bailout programme for Cyprus showed in March, almost nothing can be ruled out in this sphere either.

As far as internal risks are concerned, the central scenario of the forecast again envisages that domestic demand will decline in 2013. **Internal economic risks continue to be slightly tilted to the downside.**

The very low **level of confidence in further economic development** is persisting, although in February the business cycle indicator results in industry and among consumers suggested the possibility of a slight improvement.

So far, however, "hard" data confirm consumers' cautious behaviour and a precaution-driven (to be on the safe side should the economic situation worsen further) increase in the rate of savings. Similar situation is in the business sector, where many investment decisions are being postponed. This factor is probably the main reason explaining the "freeze" in domestic demand present in the Czech economy