Recent Economic Developments in the Czech Republic

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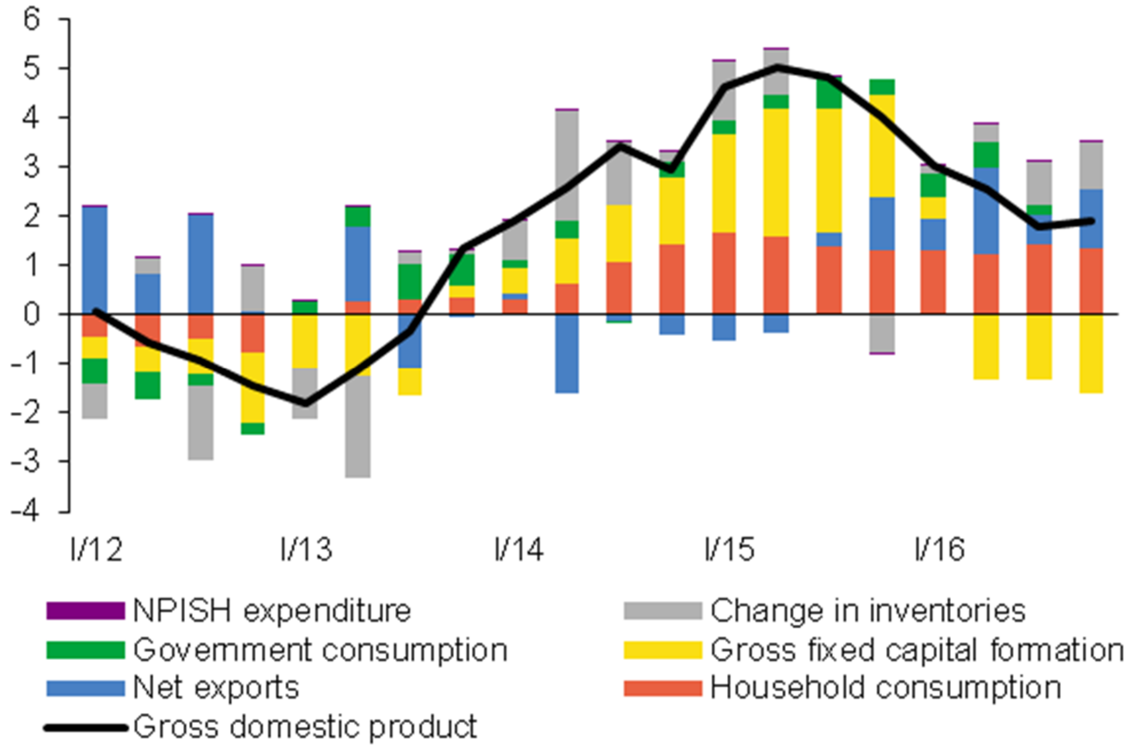
ČESKÁ ČNB NÁRODNÍ BANKA

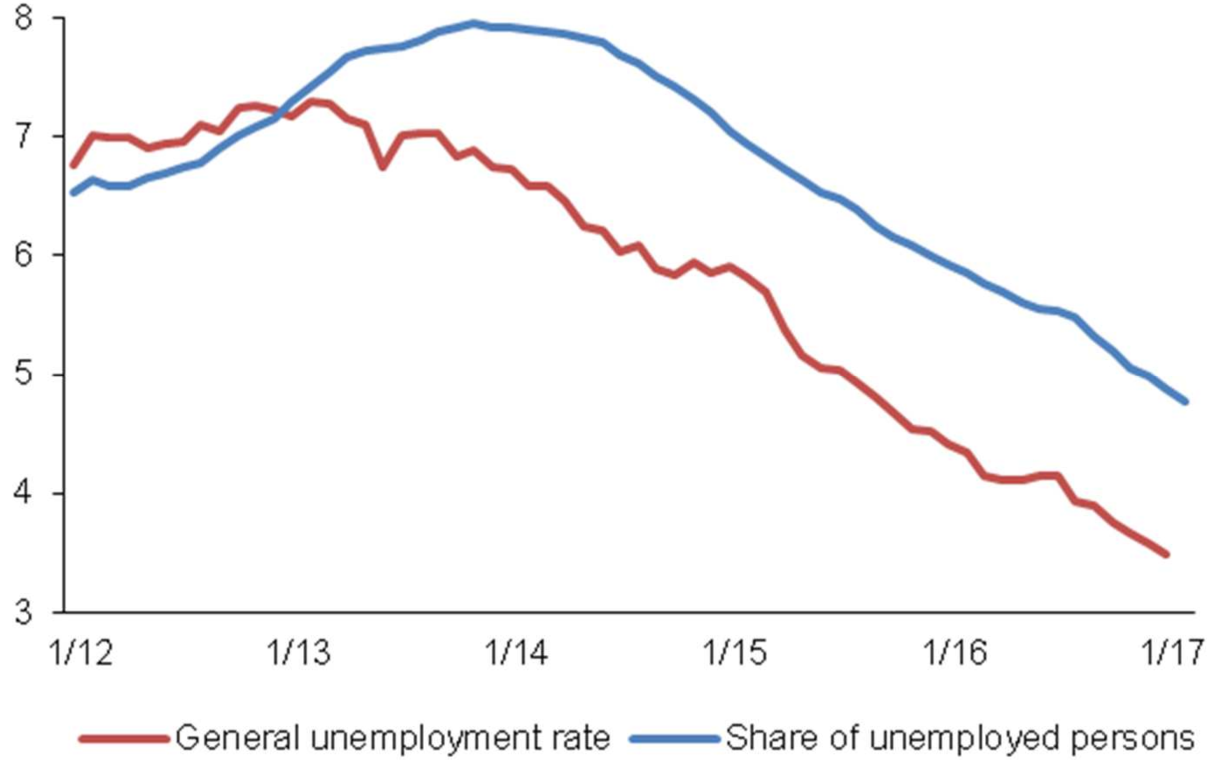
GDP
(q-o-q and y-o-y changes in % at constant prices; seasonally adjusted)



Source: CZSO

Annual GDP growth has been decelerating since mid-2015; it reached 1.9% in Q4 2016; main drivers of growth: household consumption and net exports

Unemployment indicators
(in %, seasonally adjusted)

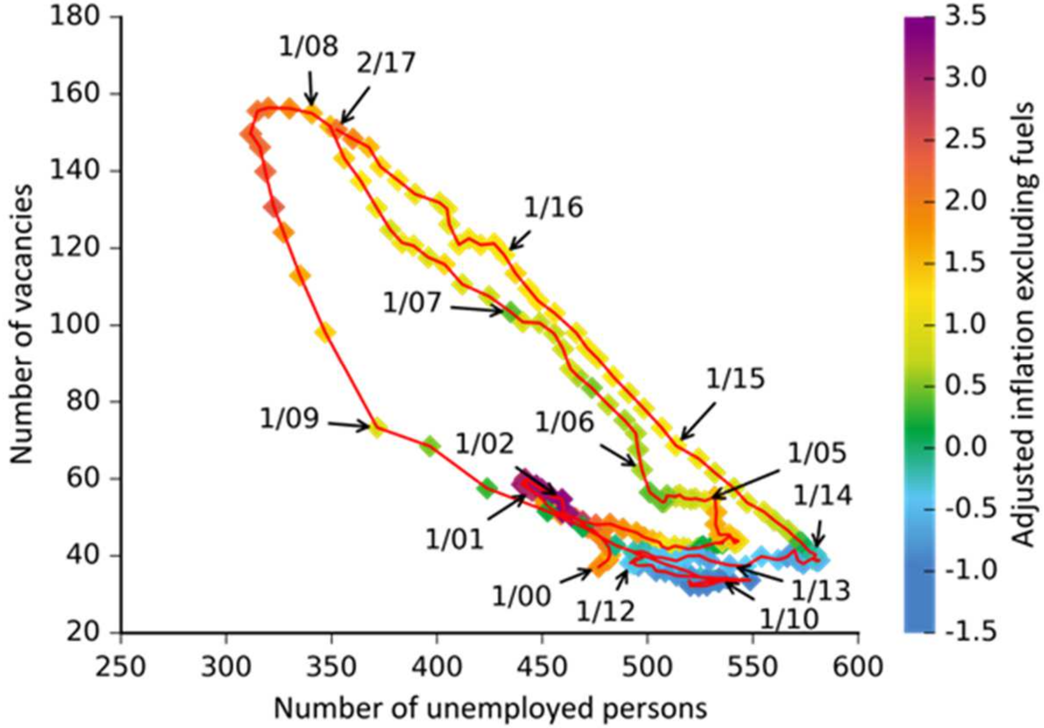


Source: MLSA, CZSO

Unemployment is falling steadily; general unemployment rate: 3.5% in January; share of unemployed persons: 4.8% in February

Beveridge curve

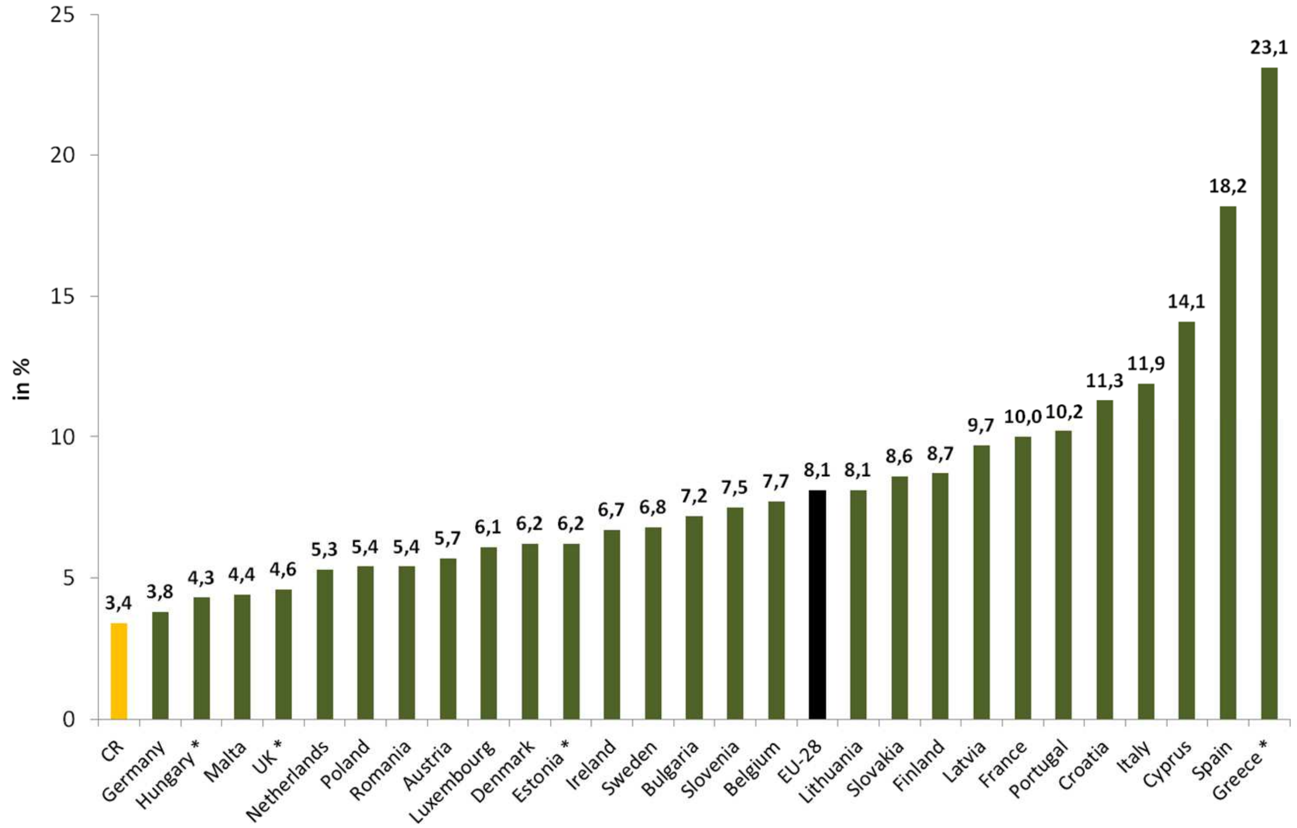
(numbers in thousands; seasonally adjusted data; annual percentage changes for adjusted inflation)



Source: MLSA, CZSO

The number of unemployed persons declined steadily, while the number of vacancies increased further; the labour market neared its 2008 peak

Unemployment in EU in Jan 2017
(as % of active population, seasonally adjusted)

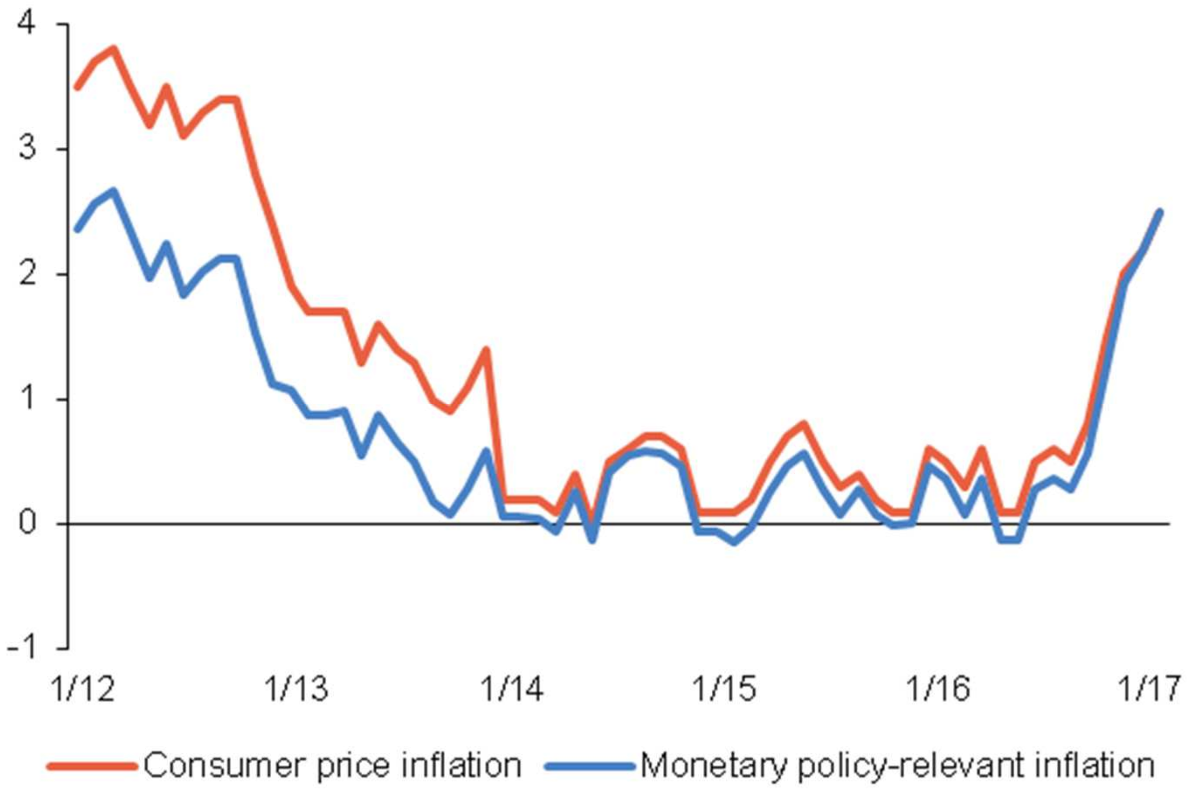


Source: Eurostat

Note: Data for December 2016 for countries marked with an asterisk

The Czech Republic currently has the lowest unemployment in the EU

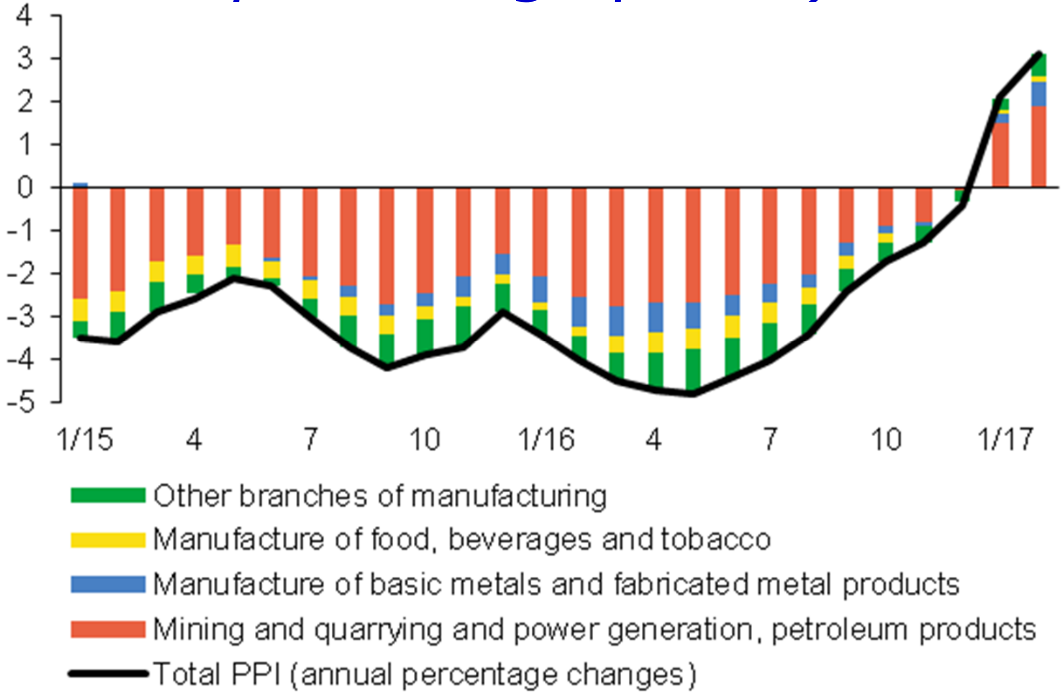
Inflation *(y-o-y changes in %)*



Source: CZSO

Consumer price inflation accelerated recently: 1.5% in November, 2% in December, 2.2% in January and to 2.5% in February (inflation target = 2%)

Industrial producer prices
(annual percentage changes; contributions in percentage points)



Source: CZSO

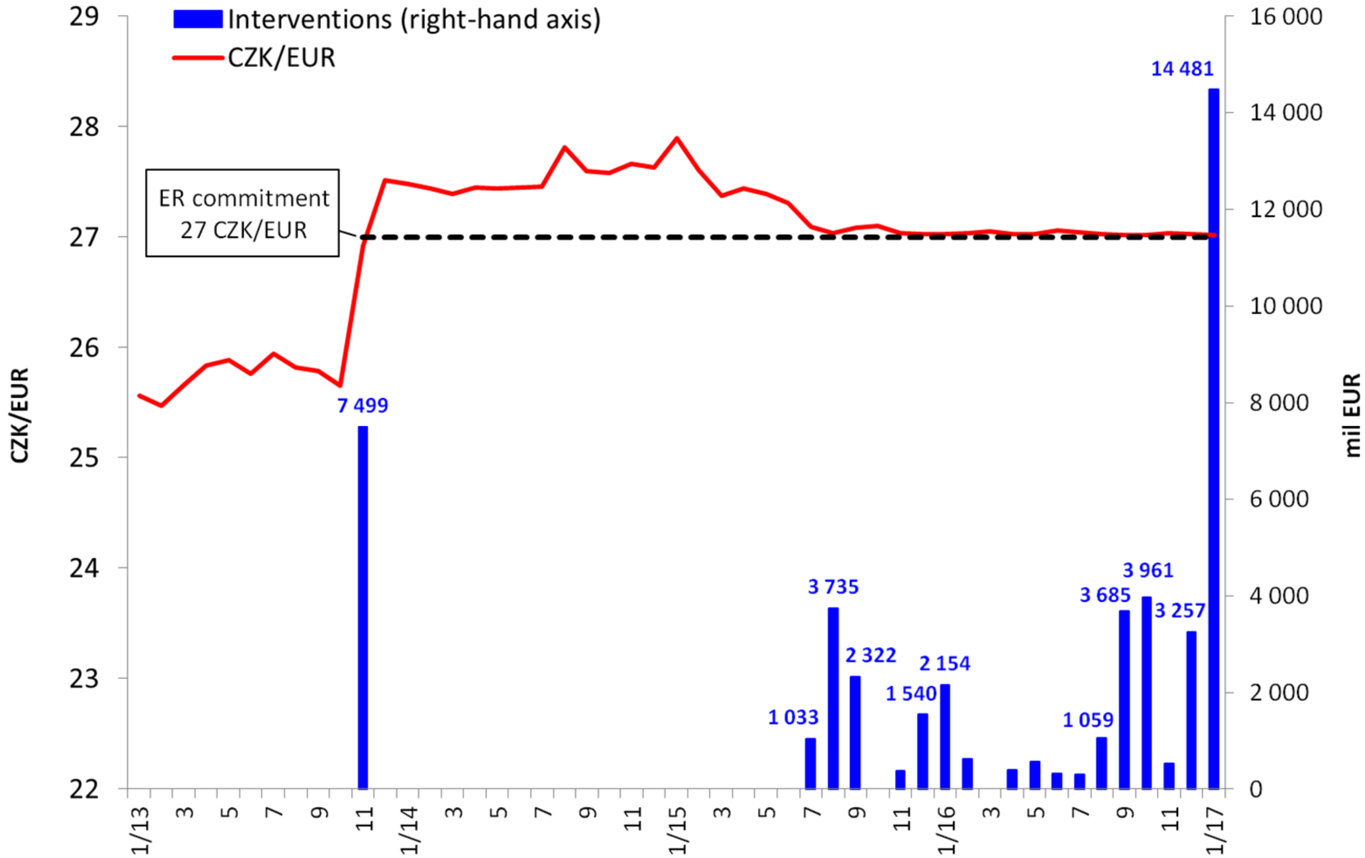
The decline in industrial producer prices moderated markedly during 2016 H2 and increased by 2.1% in January and 3.1% in February; the recent developments were driven mainly by energy prices

CNB forecast (February 2017)

	2015	2016	2017f	2018f
GDP (y-o-y %)	4.6	2.3	2.8	2.8
CPI (y-o-y %)	0.3	0.7	2.4	2.2
PPI (y-o-y %)	-3.2	-3.3	2.4	1.6
Real Wages (y-o-y %)	2.4	3.5	2.8	2.7
Employment (%)	2.2	2.1	0.7	0.3
Unemployment (ILO) (%)	5.1	4.0	3.7	3.6
Gov. deficit (% of GDP)	-0.6	0.1	0.4	0.8
Gov. debt (% of GDP)	40.3	37.6(f)	36.3	34.5
Trade balance (% of GDP)	4.1	5.3	5.0	4.9
Current account (% of GDP)	0.2	1.1	1.3	1.5

The Bank Board assessed the risks to the forecast as being balanced

Forex interventions *(Jan 2013 – Jan 2017)*



Source: CNB, Eurostat

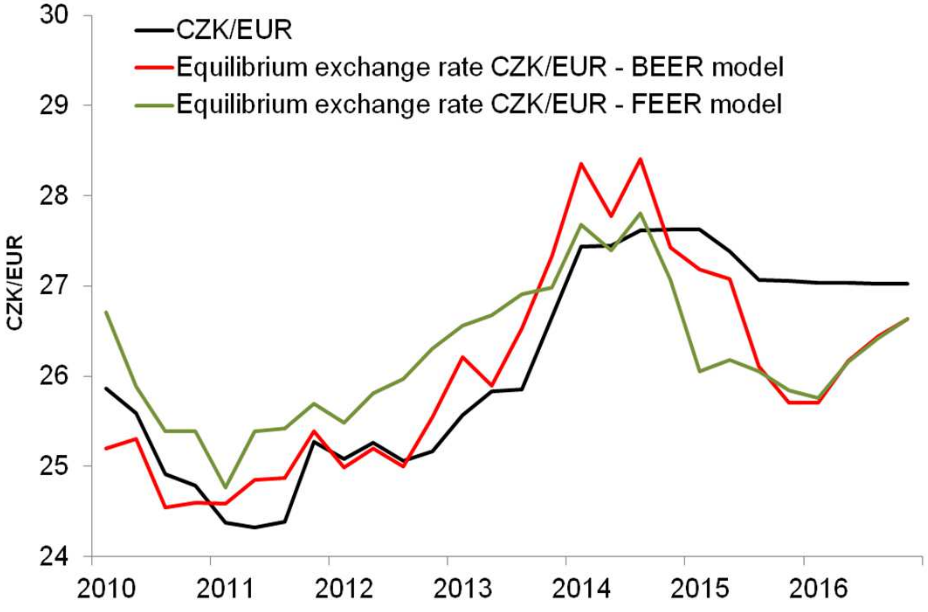
The intervention in November 2013 reached EUR 7.5 bn; cumulative interventions to defend the commitment from July 2015 to January 2017 totalled EUR 40.3 bn

Future exit from the exchange rate commitment

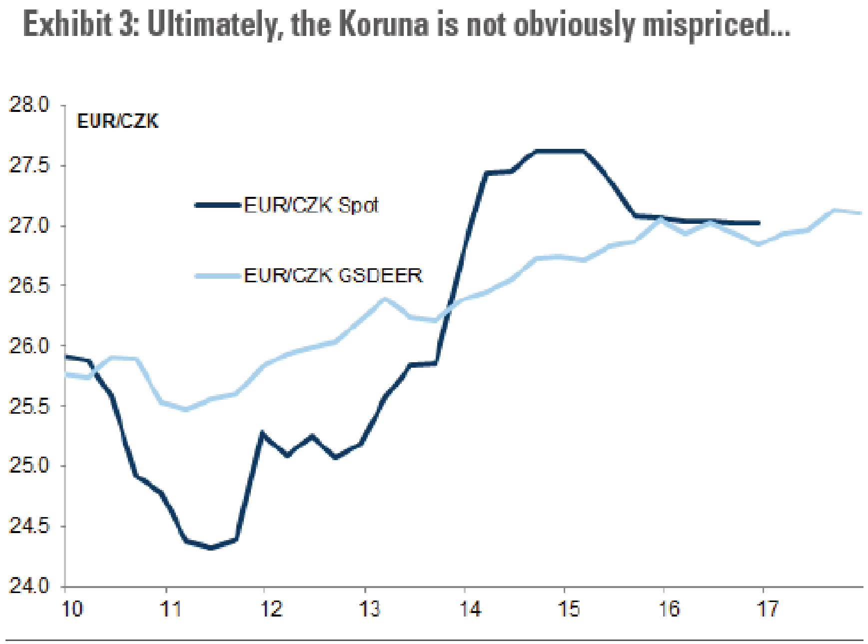
- The exit will mean that the CNB will return to the managed float regime under inflation targeting
- The exit will take place after conditions are created for sustainable fulfilment of the 2% inflation target even after the exit and there is no risk of a return to the use of unconventional measures (the CNB does not want to destabilise the economic environment: stop and go policy)
- The period of exceptional exchange rate stability, i.e. “hedging for free” provided by the CNB (macro-hedge), will end after the exit
- The execution of the exit will depend on the situation prevailing on the forex market

The meeting on 2 February 2017: *"A majority of the board members consider it likely that the commitment will be discontinued around the middle of 2017"*

Is the koruna misaligned?



Source: CNB



Source: Haver Analytics, Goldman Sachs Global Investment Research

BEER = Behavioural Equilibrium Exchange Rate
FEER = Fundamental Equilibrium Exchange Rate

According to different models, the current koruna exchange rate is close to its equilibrium

Summary

- The growth is driven by household consumption and net exports
- Unemployment is very low and the labour market is exerting upward pressure on wages (labour market: signs of overheating)
- Inflation accelerated in November–February owing to: a) food price growth, b) strengthening domestic demand pressures and c) weakening external disinflationary pressures
- Headline inflation will increase further and converge to the 2% target from above at the monetary policy horizon
- The Bank Board considers it likely that the exchange rate commitment will be discontinued around the middle of 2017
- After the exit, the koruna will probably be rather volatile for some time; it should then start to follow an appreciating trend, although more slowly than before the crisis

The exit from the exchange rate commitment will be a key event for the CNB; for the economy, it will mean a return to the exchange rate uncertainties experienced before the introduction of the commitment

Thank you

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