EmergingMarketWatch

Czech Republic Country Snapshot Reports | Oct 11, 2024

MAIN DEVELOPMENTS

KEY STATISTICS

PIRATES' DEPARTURE FROM GOVERNMENT

President Pavel appoints new ministers to cabinet

Czech Republic | Oct 08, 11:00

- **Lukas Vlcek will replace industry minister Sikela, who is joining the new EC in December**

- **Petr Kulhanek will take on the regional development ministry, after PM Fiala dismissed Ivan Bartos, the Pirates leader**
- **The resulting departure of the Pirates from the government will not impact its parliamentary majority**
- **However, it will have implications after the next general election, reducing potential allies for the current coalition**

Minister candidates confirm they will be appointed on Oct 8

Czech Republic | Oct 08, 08:09

- **Lukas Vlcek will replace Jozef Sikela as industry minister; Sikela is joining the new European Commission**
- **Petr Kulhanek will replace Ivan Bartos as regional development minister; Bartos was dismissed due to poor performance**
- **Pirates' departure from government does not jeopardize the government's majority in parliament**

STAN names Karolovy Vary governor Kulhanek as regional development minister

Czech Republic | Oct 04, 08:29

- **Kulhanek was mayor of Karlovy Vary in 2010-2018, and regional governor since 2020**
- **His priorities are repairing flood damages and the digitalisation of the building permit system**
- **PM Fiala will meet Kulhanek on Oct 4, President Pavel - on Oct 8**

New cabinet members to be appointed on Oct 8 - PM Fiala

Czech Republic | Oct 02, 18:04

- **STAN will take over the regional development ministry, should name a candidate by Thursday evening**
- **PM Fiala to meet STAN's nominee on Friday, President Pavel will meet them next Monday**
- **Pavel will also meet industry minister nominee Lukas Vlcek next week**
- **Legislation minister position will be abandoned, and foreign minister Lipavsky has already agreed to stay**

Lipavsky to remain as foreign minister, despite Pirates' departure

Czech Republic | Oct 01, 15:49

- **All four parties supported Lipavsky staying, which is what changed his mind**
- **Thus, PM Fiala has only a regional development minister to name, as he intends to remove the legislation minister position**
- **Fiala wants a candidate for regional development minister by the end of this week, a nomination by the end of next one**

Pirates expectedly vote to leave government

Czech Republic | Oct 01, 08:21

- **709 out of 894 party members vote in favour of the decision**
- **The other Pirate ministers are expected to resign on Oct 1**
- **PM Fiala said next steps will be announced on Oct 2, he could see STAN taking over regional development ministry**
- **He would rather have Jan Lipavsky remain as foreign minister, and so would KDU-CSL and TOP 09**
- **New cabinet structure likely to be announced by the middle of next week**

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2024 FLOODS IMPACT

President Pavel signs revision to 2024 budget law

Czech Republic | Oct 03, 10:30

- **State budget deficit target is now CZK 282bn in 2024 (up CZK 30bn), CZK 241bn in 2025 (up CZK 11bn)**
- **We estimate gross financing needs will reach 6.3% of GDP in 2024 and 6% of GDP in 2025**
- **General government deficit to reach 2.8% of GDP in 2024, 2.3% of GDP in 2025**

Lower house passes revision of 2024 budget law

Czech Republic | Oct 01, 19:21

- **The revision passed through an emergency legislative procedure**
- **No one objected to the revision, which completes the adoption process**
- **President Pavel may sign the revision as early as this week**

General government deficit to reach 2.8% of GDP in 2024 due to floods

Czech Republic | Oct 01, 19:04

- **General government deficit to reach 2.3% of GDP in 2025**

Government passes revisions to 2024, 2025 budgets to cover flood damage

Czech Republic | Sep 25, 17:51

- **Deficit target to rise by CZK 30bn in 2024 and CZK 11bn in 2025**
- **Additional spending to go primarily on transport infrastructure**
- **We expect general government deficit to reach 2.9% of GDP in 2024, 2.2% of GDP in 2025**

EU to provide EUR 2bn in grants as flood relief - PM Fiala

Czech Republic | Sep 20, 08:03

- **This is part of an EUR 10bn package from cohesion funds promised by EC President Von der Leyen**
- **No national co-financing will be required for flood relief**
- **Opposition ANO to back a flood bond issue, but not emergency taxes**

Govt to raise deficit target by CZK 30bn in 2024, CZK 10bn in 2025 - Stanjura

Czech Republic | Sep 19, 13:01

- **The state budget will thus see a deficit of CZK 282bn in 2024 and CZK 240bn in 2025**
- **We estimate the general government deficit will reach 2.9% of GDP in 2024 and 2.2% of GDP in 2025**
- **Stanjura ruled out emergency taxes, said only debt financing will be used to cover the extra spending**
- **It will put gross financing needs to 6.4% of GDP in 2024 and 6% of GDP in 2025**
- **The government is expected to pass the amendments to the 2024 and 2025 budgets next week**
- **It will seek emergency legislative procedure for the 2024 budget amendment, as well as seek opposition endorsement**

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BUDGET 2025

Government strikes a deal with public sector unions on wage levels in 2025

Czech Republic | Oct 03, 14:53

- **Monthly base wages will rise by CZK 1,400 across the board**
- **This is simply a rearrangement of the total planned increase, as now the bigger part will be 100% guaranteed**

Fiscal council sees possible slippage from target at 0.3-0.4% of GDP in 2025

Czech Republic | Oct 03, 14:15

- **The Council sees several problematic areas, both on the revenue and expenditure side**
- **We see one of the criticisms as a bit too hard, so the more likely slippage risk should be around 0.24-0.26% of GDP**
- **Yet, we don't expect the government to react, as 2025 is an election year**

Government and unions to meet on public sector wages on Oct 3

Czech Republic | Sep 27, 14:56

- **Unions still want a 10% increase in base wages, and an 8% increase in the wage bill**
- **The government only offers a 3.7% average wage hike, and a 5% increase in wage expenses**
- **We doubt we will see a more generous government, despite the regional election results**

Talks with unions on public sector wages to resume next week - PM Fiala

Czech Republic | Sep 26, 08:20

- **Talks were postponed due to the floods**
- **Unions still want a 10% increase in base wages, and an 8% increase in the wage bill**

Government approves pension indexation, minimum wage hike in 2025

Czech Republic | Sep 18, 17:54

- **Average pension to rise by 1.7%, lowest pension will rise by 2.6%**
- **The minimum wage will increase by 10.1%**
- **Minimum guaranteed wages will be abandoned in the private sector**

Government to vote 10% minimum wage hike in 2025 on Sep 18

Czech Republic | Sep 16, 08:17

- **The minimum wage is now set as a percentage of the average wage, so it will reach 42.4% in 2025**
- **Additional labour costs in the private sector to reach CZK 4.7bn in 2025 and CZK 4.4bn in 2026**
- **The net fiscal cost is estimated at CZK 10.1bn in 2025 and CZK 8.4bn in 2026**
- **Unions are not happy with the provisions, but they are yet to mount a major strike**

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EUROPEAN PARLIAMENT ELECTION 2024 AND AFTERMATH

STAN expectedly names Lukas Vlcek as industry minister

Czech Republic | Sep 26, 19:23

- Vlcek to replace Jozef Sikela, who is joining the European Commission
- Sikela will likely start as an EU commissioner as of Dec 1

Sikela to become EU commissioner for international partnerships

Czech Republic | Sep 17, 12:16

- The portfolio deals with promoting EU policies abroad, and mostly international development
- We consider it a lesser portfolio than the Czech Republic hoped for, though PM Fiala tried to downplay that
- Sikela will deal with security access to major markets, so there is some importance, but it is not the industry or energy portfolio

Sikela could reportedly get trade or energy portfolio in EC

Czech Republic | Sep 09, 08:21

- Sikela made a good name during the peak of the energy crisis, when he brought member states together
- Czech EU affairs minister mentioned the trade portfolio, Die Welt newspaper - the energy one
- The new European Commission could be revealed as early as on Sep 11

Government officially names industry minister Sikela as EU commissioner

Czech Republic | Aug 21, 18:13

- Sikela was also confirmed by parliament earlier on Aug 21
- The next step is to submit the nomination to EC President Von der Leyen

Chamber's European affairs committee backs Sikela as EU commissioner

Czech Republic | Aug 21, 14:42

- Cabinet needs to reaffirm nomination, which may happen on Aug 21, according to PM Fiala
- Some MPs expressed concerns why the government has not named a woman as well, like EC President Von der Leyen asked

Government unanimously nominates industry minister Sikela for EU commissioner

Czech Republic | Jul 25, 07:37

- PM Fiala wants Czech EU Commissioner to have real powers, confident Sikala can manage such portfolio, country aims at economic portfolio
- Fiala is now to submit nomination to lower house European Committee, government then to give final approval

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EURO ADOPTION

Czech Republic meets only a single euro area criteria - EC convergence report

Czech Republic | Jun 26, 14:17

- Only the interest rate criterion is met, inflation is above, and the Czech Republic has not entered the ERM-II
- The Czech Republic meets EDP criteria, even though its general government deficit was above 3% of GDP in 2023

- **Public support for euro adoption is low, which is why no steps have been made towards entering the euro area**

Czech firms to welcome euro adoption - Deloitte survey

Czech Republic | Apr 23, 15:39

- **Czech firms expect lower interest rates, lower exchange rate risk, easier trade with euro area**
- **High debt levels in some euro area members are the main concern**

Majority of firms would like euro adopted in the Czech Republic - survey

Czech Republic | Apr 10, 08:45

- **77% of respondents want the euro, 88% would have it ideally within the next 5 years**
- **Greater mobility and free movement are considered the biggest benefits of EU membership**
- **More regulations and red tape are the biggest cons**

Government doesn't set a euro adoption date, as expected

Czech Republic | Feb 14, 17:03

- **ODS remains firmly opposed to euro adoption, even if other ruling parties support it**
- **Finance ministry report on euro adoption is more mellow now than in previous years**
- **Monetary policy transmission risks are now considered moderate, with insufficient convergence to euro area economies being the main risk**
- **We expect euro adoption to remain a primarily political issue; however, a debate has started in earnest, something that was not the case prior to 2024**

Ruling coalition decides to downgrade euro adoption coordinator to advisor

Czech Republic | Feb 07, 07:52

- **New status means the position will have no direct access to the cabinet**
- **PM Fiala agrees to have the government's economic advisory team prepare a report on ERM membership, to be ready in October**
- **While the issue is probably off the agenda in the current electoral cycle, we feel political debate about euro adoption has started in earnest**

STAN minister stirs government by appointing euro adoption co-ordinator

Czech Republic | Feb 06, 07:59

- **Position has been vacant since 2017**
- **Debate on euro adoption has been non-existent until recently, when President Pavel urged the government to finally do something**
- **ODS is the only party in government to oppose euro adoption, it called for a coalition debate on the issue**
- **We don't expect serious fractures in the government, but any euro adoption effort is likely to be frustrated**

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RUSSIA'S INVASION OF UKRAINE

Natural gas storages 93.3% filled as of Sep 6 - Sikela

Czech Republic | Sep 09, 08:30

- **Consumption is lower, down 22.5% compared to 2019-2023 average**
- **European storages were filled at 92.8% as of Sep 4 on avearge**

Czech Republic to withstand suspension of Druzhba oil pipeline as of 2025

Czech Republic | Aug 30, 15:21

- **We believe the remark refers to the connection to the TAL pipeline, currently being built**
- **Czech representative said it was not the first time Ukraine has brought up the possibility that the pipeline may stop**

Czechs to use part of confiscated Russian assets to buy munitions for Ukraine

Czech Republic | Aug 20, 11:35

- **Defence minister Cernochova did not mention what amount of money will be raised, probably due to security concerns**
- **The munitions initiative has already delivered 50,000 artillery rounds to Ukraine, with the goal being 500k by end-2024**

Czech Republic to get 14 more Leopard tanks for donations to Ukraine

Czech Republic | Jul 31, 15:10

- **The first 2A4 tank should be delivered by the end of 2024, the rest - by early 2026**
- **Germany already donated 14 2A4 Leopard tanks in 2022-2023**
- **Technical consultations on the purchase of 2A8 Leopard tanks also took place**

PM Fiala, Ukrainian President Zelensky sign 10-year security agreement

Czech Republic | Jul 18, 18:17

- **Accord envisages Czechia training Ukrainian soldiers, Ukraine to provide assistance in event of military attack on the Czech Republic**
- **Agreement not legally binding, PM Fiala views it as important symbol, diplomatic sources say new Czech government may rescind it**

Ukraine to build ammunition factory with Czech help – Ukrainian PM Shmyhal

Czech Republic | Jul 16, 18:28

- **PM Fiala promise Czech Republic to help Ukraine modernise its nuclear reactors and build new ones, to continue ammunition drive next year as well**

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POWER AND GAS PRICE CHANGES

CEZ to lower electricity, natural gas prices on no-fixation contracts as of 2025

Czech Republic | Sep 03, 12:03

- **Electricity prices to fall by 6%, natural gas prices - by 10%**
- **CEZ claims 1.7mn customers will be impacted, but we doubt the number is accurate**
- **PRE lowered energy prices for customers without a fixed price plan as of September, claims 700k customers will be affected**
- **E.ON is lowering natural gas prices by 12% as of October, to impact 150k customers**
- **We estimate the inflation impact of PRE's price cut at -0.16pps, E.ON's at - 0.01pps, and CEZ's - at -0.16pps**

Czechia accuses Germany of hoarding gas meant to supply Czech Republic

Czech Republic | Jul 19, 07:06

- **Sikela sent letters to EU Commissioner for Energy Simson, German economic minister Habeck**

PRE to lower power prices by 20% as of September, natural gas prices - by 16%

Czech Republic | Jul 02, 13:36

- **PRE covers about 700k households, and if all see price cuts, the impact on headline CPI inflation will be about -0.19pps**
- **Other suppliers have announced price cuts as well, so if prices fall at this rate nationwide, the impact on inflation will be -1.2pps**
- **However, we don't believe the cuts apply to fixed price plans, which is why we expect the impact on inflation to be lower**

Fixed electricity price plans are slightly cheaper, but it may end soon

Czech Republic | Apr 19, 08:24

- **Spot prices are about to decrease slightly, allowing for better offers**
- **Fixed price plans for 1 or 2 years see about a 9-10% decrease in final prices**
- **However, energy firms anticipate that wholesale electricity prices will only rise from here on**
- **Given that there is a time lag before wholesale prices affect retail prices, fixed price plans may remain lucrative until this autumn**

Energy regulator approves a sharp hike of regulated energy prices in 2024

Czech Republic | Nov 30, 14:32

- **Regulated component of electricity prices will rise by 65.7%, of natural gas prices - by 38.8%**
- **The main reason is the expiration of the renewable energy surcharge waiver at the end of 2023**
- **Regulated prices will thus have a weight of 39% for electricity and 20% for natural gas**
- **We estimate a net impact of +0.22pps on headline inflation, out of which +0.53pps from electricity prices**

Industry minister with two proposals how to lower energy prices in 2024

Czech Republic | Nov 20, 08:34

- **One is to allow the energy regulator to adjust regulated charges more frequently than once a year**
- **Another is to extend the renewable energy surcharge waiver to certain consumers**
- **The second measure is to be funded by carbon credits, but the EC may not allow it**

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DUKOVANY NUCLEAR PLANT EXPANSION

Czech firms to receive orders for CZK 240bn in Dukovany power plant expansion

Czech Republic | Sep 20, 16:51

- **The big orders promised to local firms likely gave KHNP victory in the nuclear expansion tender**

Impact study on new nuclear units to be ready in October - PM Fiala

Czech Republic | Sep 03, 08:01

- Government plans to invest CZK 14bn in transport infrastructure around the plant over the next decade

EDF appeals KHNP victory in nuclear power expansion tender

Czech Republic | Aug 27, 14:47

- EDF challenges the tender procedure
- Westinghouse challenged the choice back in July, arguing winner KHNP doesn't have rights to the technology
- CEZ remains confident that the procedure is solid and will withstand appeals

CEZ opens talks with KHNP on contract to build two units at Dukovany n-plant

Czech Republic | Jul 25, 07:45

- Contract expected to be signed by end-March 2025
- Czech companies to participate in about 60% of this strategic investment

US Westinghouse claims KHNP not entitled to use technology offered for Dukovany

Czech Republic | Jul 18, 07:21

- Westinghouse plans to defend itself legally as well

Government chooses Korean KHNP to build two new units in Dukovany n-plant

Czech Republic | Jul 17, 16:47

- PM Fiala says KHNP's offer was better than that of French EDF in terms of all evaluation criteria
- One block to cost CZK 200bn at current prices, budgetary costs for preparatory work for new units in Dukovany to total CZK 80-85bn in next five years
- Construction to start in 2029, trial operation of first new unit planned for end-2036, commercial operation is scheduled to begin in 2038
- EC already approved state aid in form of loan for construction of one unit, FinMin Stanjura to submit request for state aid for second unit asap
- Share of nuclear energy in energy mix to increase by 9pps to 46% with two new units
- Government will negotiate with KHNP to build two new units at Temelin n-plant as well

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PENSION REFORM

Maximum retirement age not to exceed 67 years - Jurecka

Czech Republic | Oct 03, 08:00

- The government already eased the maximum increase in the retirement age to one month annually
- However, no retirement age cap was set, which will now change
- Labour minister Jurecka did not mention how the impact from pension reform will change
- He also promised employment support to firms whose activity has been impeded by the floods

Ruling coalition agrees to slow down increase in retirement age

Czech Republic | Aug 29, 16:25

- Under the current version of pension reform, the retirement age may rise by up to two months every year
- The new proposal will cap the pace of increase to one month at most
- The change is expected to reduce the projected savings from pension reform by about 0.3-0.4% of GDP, down to about 1.7-1.8% of GDP annually

Government plans a slower increase in retirement age

Czech Republic | Aug 28, 08:31

- The retirement age was tied to life expectancy changes, but the government wants to slow down the pace of increase
- Labour minister Jurecka estimates the amendment will have a fiscal impact of 0.4% of GDP, thus putting reform-caused savings to about 1.7% of GDP annually
- Jurecka also confirms the government intends to raise public sector wages in 2025, doesn't provide more details

Jurecka promises final agreement on pension reform by end of summer break

Czech Republic | Aug 05, 08:20

- The goal is to avoid the risk of rolling back the reform after the next general election
- Yet, consensus appears to be still far, as everyone pushes in their direction

Retirement age allegedly to be raised more slowly than planned – daily

Czech Republic | Jul 18, 07:33

- Coalition is now deciding between several options, including original one, all of them do not differentiate between women and men
- Government expert group to continue discussion in August as no agreement was reached, experts mostly liked capping retirement age at 67 years

Coalition has to agree on possible changes to pension reform by fall – Jurecka

Czech Republic | Jul 15, 07:26

- Labour minister wants debate on form of changing retirement age, other measures to be concluded by end-August
- Second reading of pension reform can be held in September or October

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EUROBOND ISSUANCE

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KEY STATISTICS

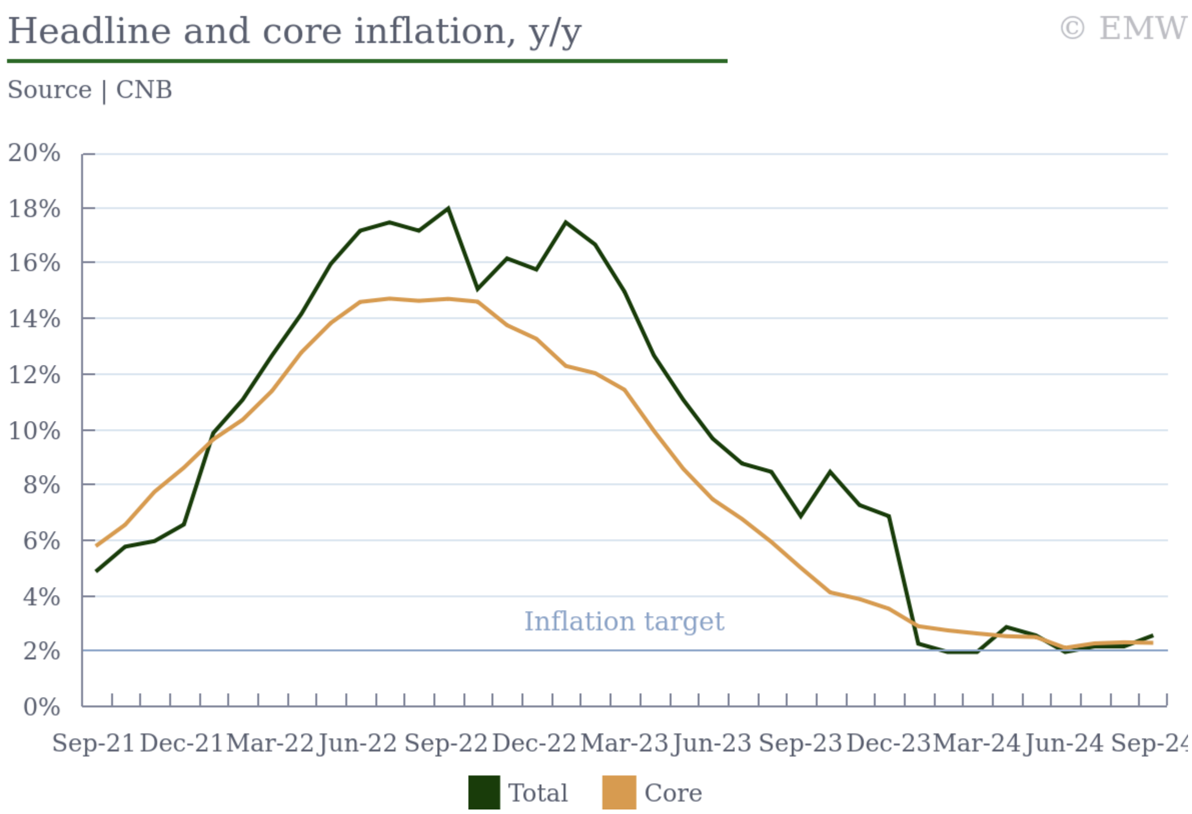
Core inflation eases to 2.3% y/y in September, below projection

Czech Republic | Oct 10, 14:38

- The CNB expected core inflation at 2.4% y/y
- As expected, food prices surprised the most on the upside
- Regulated prices also rose faster than expected, but their impact was negated by fuel prices

- **Food prices were the major factor behind stronger-than-expected inflation in Q3, while core inflation was only marginally stronger**
- **With that in mind, we expect that the CNB will deliver a 25bp cut in November but may pause in December if headline prints go higher**

Core inflation eased to 2.3% y/y in September from 2.4% y/y in August, according to figures from the CNB. The print was slightly below the CNB's projection, which suggested core inflation would end up at 2.4% y/y. This puts even more emphasis on the impact of volatile prices on the deviation of headline CPI inflation from the forecast, at 0.3pps in September. We remind that headline inflation accelerated to 2.6% y/y in September, compared to the CNB's forecast of 2.3% y/y. However, this was exclusively due to volatile prices, which particularly stands out in Q3 data. Headline CPI inflation was 2.3% y/y in Q3 2024, or 0.3pps above the CNB's forecast. Yet, core inflation was responsible for only 0.03pps of that deviation (or one tenth), ending up only about 0.05pps above the CNB's projection.



Data Download

The CNB breakdown confirmed what we saw in the statistical office's release, namely that it was food, beverage, and tobacco prices that surprised on the upside. That measure reported an increase of 2.6% y/y in September, compared to 1.1% y/y anticipated by the CNB. There was also a discrepancy with regulated prices, which rose by 6.6% y/y, 1pp faster than expected. However, their impact was completely mitigated by fuel prices, which fell by 11.3% y/y, compared to a CNB projection for a 5.9% y/y fall. Thus, it is effectively food prices that the CNB's forecasting model has a serious trouble with. It was also that category that contributed the most to the deviation of headline inflation in Q3, by 0.26pps.

CNB staff continue to expect no major deviation from the 2% target, either in the rest of 2024 or in subsequent years. Yet, we remind that the latest CNB forecast expects CPI inflation at 2.3% y/y in Q4 2024, which is 0.3pps higher than the forecast for Q3 2024. If we assume the same deviation, it would imply that CPI inflation could be slightly above 2.5% y/y in Q4, with some monthly prints nearing 3% y/y. We will see a new forecast next month, however, which may adjust inflation projections, so we recommend that you consider the summer forecast a bit outdated, as far as the headline measure is concerned.

Monetary policy impact

The core inflation print reinforces our expectation that the CNB board will deliver one more 25bp cut in November. While the headline doesn't look good, it is clearly driven by volatile, and mostly food prices, whose impact has been downplayed before. Core inflation has been more or less in line with the forecast, and we expect this to be a strong argument in favour of easing monetary conditions further. However, we expect that board members will be uneasy with the high headline print regardless, which may cause a pause in December. We expect headline CPI numbers in Q4 2024 will be instrumental for such a decision, and both the October and November CPI prints will be available before the last MPC meeting in 2024, on Dec 19. Thus, the board will have enough information to decide whether it is better to wait a bit, or go for another 25bp cut.

In any case, even if the CNB pauses in December, we expect at least one more 25bp cut in 2025, with two or three being more likely. That part will depend on how the economy develops, as sustained low external demand will likely allow the CNB to extend the easing cycle more than it currently implies. Thus, the most likely scenario, at least for now, appears to be a policy rate at 4% at the end of 2024, and then two to three 25bp cuts in H1 2025, after which the easing cycle will likely end.

CNB inflation measures

	Sep-23	Jun-24	Jul-24	Aug-24	Sep-24
Change, y/y					
Total	**6.9%**	**2.0%**	**2.2%**	**2.2%**	**2.6%**
Regulated prices	15.3%	5.7%	5.4%	5.2%	6.6%
Food, beverages and tobacco	6.0%	-0.8%	-0.1%	1.0%	2.6%
Core inflation	**5.0%**	**2.2%**	**2.3%**	**2.4%**	**2.3%**
Fuel	-6.6%	5.0%	4.6%	-4.2%	-11.3%
Monetary policy-relevant inflation	**6.7%**	**1.9%**	**2.1%**	**2.1%**	**2.5%**
Contribution to y/y dynamics, pps					
Regulated prices	-1.00	-0.03	-0.04	-0.03	0.21
Food, beverages and tobacco	-0.41	-0.19	0.18	0.29	0.43
Core inflation	-0.52	-0.21	0.09	0.02	-0.01
Fuel	0.21	-0.16	-0.01	-0.31	-0.28

Source: CNB

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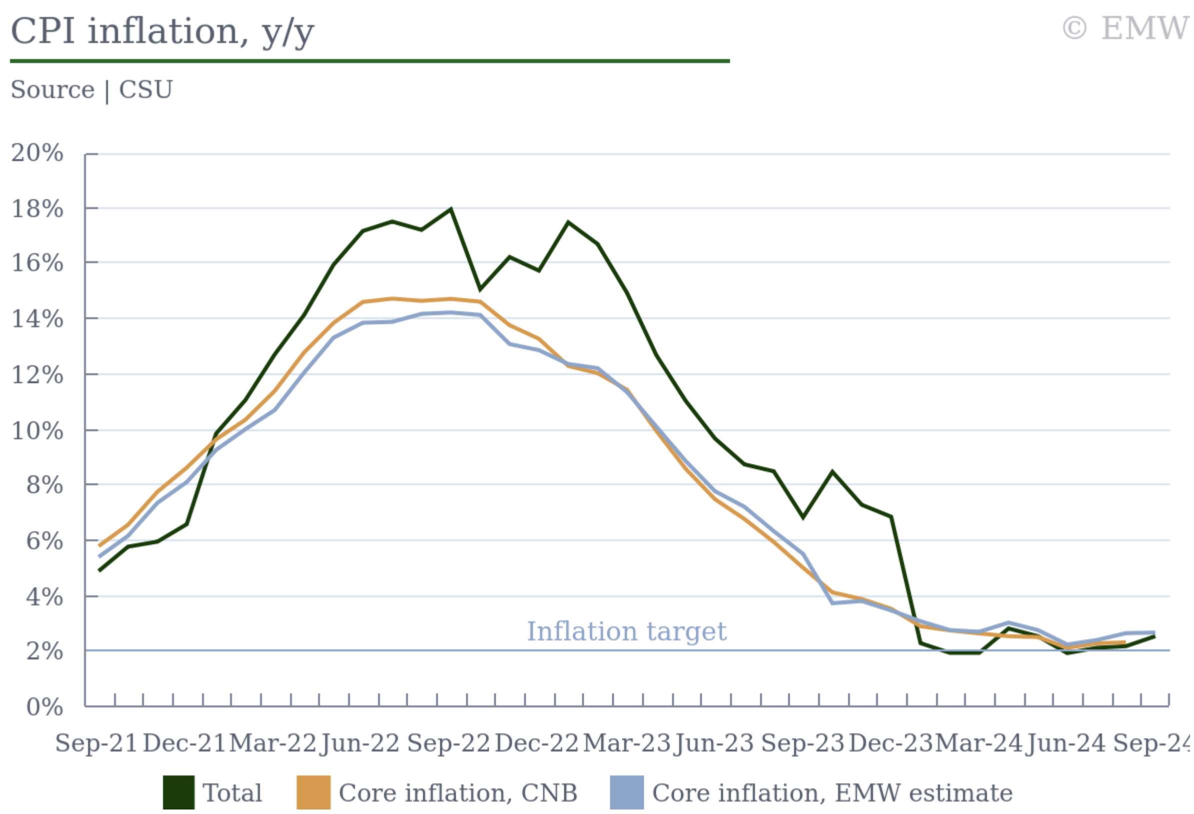
CPI inflation surprises on the upside, accelerates to 2.6% y/y in September

Czech Republic | Oct 10, 10:38

- **Markets expected inflation at 2.4% y/y, the CNB - at 2.3% y/y**
- **Food prices were the main reason for stronger inflation**
- **Energy prices had an upward impact due to base effects, but it was fully mitigated by fuel prices**
- **We estimate that core inflation remained flat in September, which would still put it 0.2pps above the CNB's forecast**
- **We still doubt the CNB board will pause in November, but the odds for a pause in December are now higher**

CPI inflation surprised on the upside, accelerating to 2.6% y/y in September from 2.2% y/y in August, according to figures from the statistical office. Market expectations were for inflation at 2.4% y/y, which was still above the CNB's forecast of 2.3% y/y. As a result, CPI inflation averaged 2.3% y/y in Q3 2024, which is

0.3pps above the CNB's projection. Consumer prices fell by 0.4% m/m in September, against market expectations of a 0.5% m/m fall.



Data Download

While the headline print appears troubling, the factors behind it paint a somewhat different picture. The primary growth driver for headline inflation was food prices, which turned from a 1.8% y/y fall in August to a 0.6% y/y increase in September, being the biggest upside surprise. Food prices also rose by 0.8% m/m in September, which was their strongest increase since April, and not very typical for a September. Thus, we expect that food prices will be the category that has deviated the most from the CNB's projections. There was also an upside push from energy prices, though it was anticipated, as it was mostly a base effect, as energy prices decelerated their growth sharply in September 2023. Yet, it was fully mitigated by fuel prices, whose decline strengthened to 11.9% y/y, the strongest since the middle of 2023. There was also some pressure from seasonal goods, but overall, nothing outside the factors listed above.

As a result, we estimate that core inflation remained flat in September, which will likely impact the CNB board's assessment of the CPI print. We should note that even then, core inflation has been slightly stronger than the CNB's projections. At the end of the day, if it is volatile prices that are pushing the headline upwards, their importance will be far less if the main factor was core inflation.

Monetary policy impact

We are still to see the breakdown of core inflation, but it appears that it was once again food prices that boosted headline inflation above expectations. In that case, we expect that reaction from the CNB board will be limited. If our estimate is accurate, core inflation will have ended up 0.2pps above the CNB's forecast in Q3 2024, which is not a desired development, but not a particularly dire one. As far as the headline is concerned, it was indeed 0.3pps above the Q3 forecast, but at least half of it was due to food prices, which the CNB's forecasting model has had a particular difficulty predicting recently.

Thus, we doubt that we will see a pause in monetary easing so early. Real interest rates remain positive even after the latest 25bp cut, even though they are nearing a level that many expect the CNB will pick as the moment to enter the current policy cycle. Historically, real interest rates have been targeted at around 1%, but now, it appears that the target will be around 1.50%. The real monetary policy rate reached 1.64% in September, which under current circumstances would imply only one more 25bp cut, and then a pause until inflation eases back to the 2% target. Thus, it appears that a lot will depend on the next CNB staff forecast, which is due at the next MPC meeting on Nov 7. If the inflation projection worsens, then the odds for a pause in December will increase considerably. Given how the board has currently positioned itself, it appears a likely scenario to have the policy rate end 2024 at 4%.

CPI inflation, % y/y

	Sep-23	Jun-24	Jul-24	Aug-24	Sep-24
Total	**6.9%**	**2.0%**	**2.2%**	**2.2%**	**2.6%**
Food and non-alcoholic beverages	6.0%	-4.2%	-3.1%	-1.8%	0.6%
Alcoholic beverages, tobacco	6.9%	4.9%	4.5%	4.7%	4.6%
Clothing and footwear	9.2%	2.9%	2.2%	1.9%	1.2%
Housing, water, energy, fuel	8.9%	3.0%	3.0%	3.0%	3.7%
Furnishings, household equipment	3.7%	-0.1%	0.3%	0.4%	1.1%
Health	8.8%	3.8%	3.9%	4.1%	3.8%
Transport	0.2%	3.7%	3.7%	1.0%	-1.8%
Post and telecommunication	4.3%	2.1%	0.6%	0.8%	0.9%
Recreation and culture	8.7%	2.6%	3.3%	3.7%	3.2%
Education	6.5%	6.5%	6.5%	6.6%	11.3%
Restaurants and hotels	10.3%	7.5%	7.4%	7.0%	7.1%
Miscellaneous goods and services	6.9%	2.9%	3.9%	3.4%	3.6%
Core inflation, EMW estimate	5.5%	2.3%	2.4%	2.7%	2.7%
Core inflation, CNB	5.0%	2.2%	2.3%	2.4%	-
Tax adjustments	0.2%	0.1%	0.1%	0.1%	0.1%
Administered prices	2.6%	0.8%	0.8%	0.7%	1.0%
Core inflation	4.0%	1.1%	1.3%	1.4%	1.5%
Seasonal effects	-2.5%	-0.7%	-0.4%	-0.1%	0.0%
Core inflation, sa	6.5%	1.8%	1.7%	1.6%	1.5%

Source: Czech stats office

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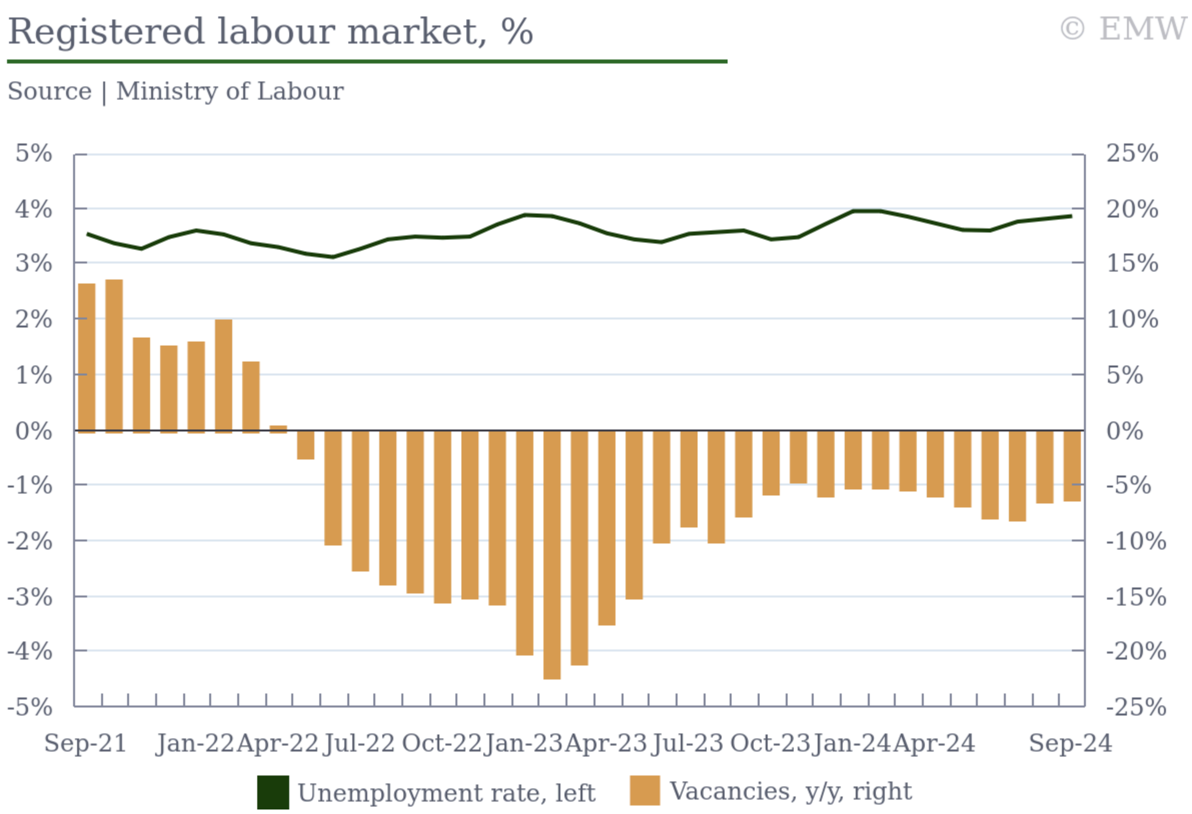
Registered unemployment rate reaches 3.9% in September

Czech Republic | Oct 08, 10:48

- **Markets expected the unemployment rate at 3.8%**
- **Vacancies-to-jobseekers ratio improves bit but remains high at 0.91**
- **People finding employment still rise fast, though newly registered jobseekers were still higher**
- **We expect the labour market to remain in stagnation, as it is still too tight, even under conditions of weak demand**

The registered unemployment rate (15-64 years) reached 3.9% in September, according to figures from the labour ministry. The print was slightly above market expectations, which put the unemployment rate at 3.8%. Yet, considering that the unemployment rate moved from 3.82% in August to 3.87% in September, it was not a big deviation. In year-on-year terms, the unemployment rate increased by 0.3pps, which reflects lower external demand that has been hitting employment in industry and transportation. The number of registered jobseekers rose by 10.6% y/y in September, and it has been two consecutive years of uninterrupted growth. The share of people receiving unemployment benefits eased to 28.9%, its lowest level in the past 11 months, indicating that the increase in jobseekers was less about new unemployment but due to long-term unemployment. We remind that staying registered as a jobseeker grants state-covered healthcare, which is a strong incentive for people to remain registered, even if their benefits expire. In contrast, the number of available vacancies fell by 6.1% y/y, even though it was their softest decline in the past 5 months. It put the vacancies-per-jobseeker ratio at its lowest level in the past 7 months, at 0.91 in September.



Data Download

The number of newly registered jobseekers rose by 10.5% y/y in September, which was a relatively solid number, likely reflecting the sustained redundancies in manufacturing. In comparison, people taken off unemployment rolls increased by 5.8% y/y, the biggest part of them due to finding employment, where the increase was 17.2% y/y. In fact, the increase in people finding employment was stronger than the increase in newly registered jobseekers, which has been encouraging. The slower decline in jobseekers was mostly due to fewer people being taken off because of administrative or other reasons, which could imply either looser oversight, or simply fewer people staying registered when they shouldn't have.

Newly announced vacancies rose by 0.8% y/y in September, which was their first increase in 11 months. The increase was a very modest one, however, and it didn't change the big picture. Lay-offs decreased by 12.3% y/y, but their number remained close to newly announced vacancies in absolute terms, which mitigated their year-on-year increase. Moreover, newly vacated positions remain very few, as there has been mostly a stagnation in the domestic labour market, with most companies bracing up during this period of low demand. Still, there were more gains in vacancies than losses, which is why the rate of decline in total vacancies eased a bit in September.

Overall, labour market tightness has been easing, but not quickly. It is indicative how, even under circumstances of low demand and marginal growth, the registered unemployment rate has remained within 4%. While we expect some further increase in Q4 2024, we doubt it will be a considerable one. There is still optimism about early 2025 bringing some improvement in external demand, which may push unemployment downwards. We doubt that will be the case, but even then, the odds are we will still see unemployment levels remaining relatively stable.

Registered labour market, %

	Sep-23	Jun-24	Jul-24	Aug-24	Sep-24
Unemployment rate (15-64 years)	**3.6%**	**3.6%**	**3.8%**	**3.8%**	**3.9%**
Vacancies per jobseeker	1.07	0.97	0.93	0.92	0.91
Receiving unemployment benefits, share	27.9%	29.3%	30.9%	30.9%	28.9%
Change y/y					
Unemployed	2.6%	9.2%	9.3%	9.8%	10.6%
o/w: available to start work	3.1%	10.7%	10.7%	11.1%	11.9%
Receiving unemployment benefits	-1.6%	13.8%	14.5%	13.9%	14.7%
o/w: available to start work	-1.2%	15.1%	15.5%	14.7%	15.7%
Job vacancies	-7.9%	-8.1%	-8.3%	-6.4%	-6.1%
Newly registered job seekers	-3.2%	-0.5%	12.9%	0.6%	10.5%
Job seekers taken off registry	1.9%	-7.4%	12.9%	-3.7%	5.8%
o/w: found employment	3.2%	9.1%	34.1%	15.5%	17.2%
Newly announced vacancies	-11.2%	-18.5%	-2.9%	-5.2%	0.8%
Filled-in positions	4.9%	-21.9%	-2.3%	-18.7%	-17.9%
Layoffs	-38.9%	-5.6%	-10.2%	-38.1%	-12.3%
Newly vacated positions	9.2%	-97.3%	-99.0%	-99.5%	-99.4%

Source: Ministry of Labour

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Retail sales rise by 5.3% y/y in August, stronger than expected

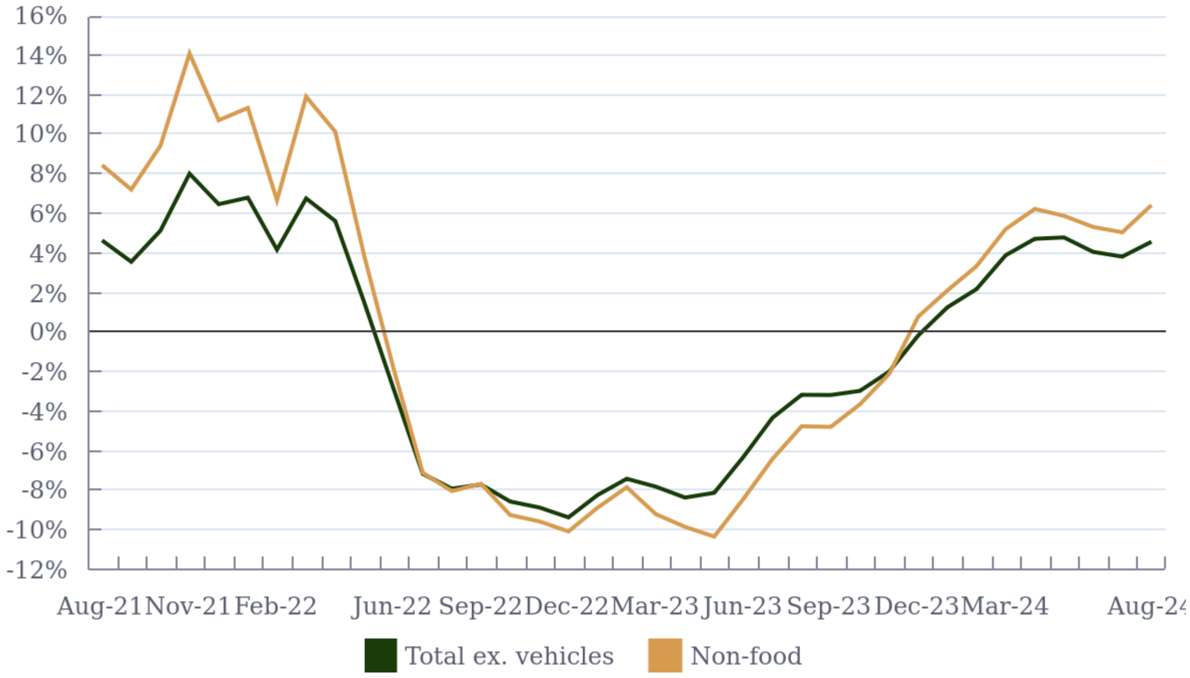
Czech Republic | Oct 08, 10:28

- **Markets expected a 4.4% y/y increase**
- **Fuel sales improved considerably, likely due to lower prices**
- **Non-food sales showed a very broad recovery, indicating that household spending is indeed on the rise**
- **Yet, we are not convinced that the recovery in household consumption will match the CNB's projection of a 2.6% y/y growth in Q3 2024**

Retail sales (excluding vehicles) rose by 5.3% y/y (wda) in August, up from 4.9% y/y in July (revised from 4.5% y/y), according to figures from the statistical office. The print was much stronger than anticipated, as markets expected an increase of 4.4% y/y. Retail sales rose by a modest 0.1% m/m (sa) in August, which was the weakest month-on-month increase in the past 3 months.

Retail sales, % y/y 3mma wda

Source | CSU



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The big boost in retail sales came from fuels, where sales rose by 9.3% y/y in August, up from only 1.5% y/y in July. This may have been caused by a relatively strong decline in fuel prices, which fell by 2.2% m/m in August and turned from a 5.6% y/y increase in July to a 4.1% y/y fall in August. Yet, non-food sales also had a strong performance, as they strengthened their increase to 7.2% y/y in August, faster by 0.6pps m/m and the strongest in the past 4 months. Regarding the various observed categories, improvement was reported almost everywhere, the only exception being cultural & recreational goods and pharmaceuticals. It would imply a steady recovery in household spending in Q3 2024, and a stronger one than in H1 2024. Online sales have also been soaring in 2024 thus far, rising by at least 14% y/y in each month of the year, and up by 16.1% y/y in August.

The only major category that saw deterioration was food & beverage sales, which eased their increase from 3.8% y/y in July to 1.6% y/y in August. The reason was most likely higher food prices, which were the primary reason why CPI inflation surprised on the upside in August. Still, food sales have increased in each month of 2024 thus far, showing a clear recovery.

The data is undoubtedly piling up towards a more hawkish stance of the CNB, as household consumption is showing clear recovery signs, and likely a stronger increase than in Q2 2024. However, the CNB already expects a pretty hefty increase in household consumption, at 2.6% y/y in Q3 2024, and we are still not convinced that actual data will match the forecast. Thus, it may turn out that even though household spending has strengthened, the acceleration is still below the CNB's forecast, which would likely soothe the concerns of some CNB board members. Given how investment is clearly struggling, the recovery in household consumption will likely have its inflationary impact mitigated through producer and service provider prices. Thus, we don't believe the August retail print immediately points towards a pause in monetary easing soon, as it will largely depend on how headline and core inflation deviate from projections.

Retail sales, y/y wda

	Aug-23	May-24	Jun-24	Jul-24	Aug-24

Total	**0.3%**	**2.1%**	**2.9%**	**2.9%**	**3.6%**
Vehicles	8.6%	0.3%	1.6%	-1.4%	-0.4%
Ex-vehicle	**-2.9%**	**3.0%**	**3.6%**	**4.9%**	**5.3%**
Food, beverages and tobacco	-4.2%	4.1%	1.7%	3.8%	1.6%
Non-food	-4.1%	3.1%	5.6%	6.6%	7.2%
Retail sale in non-specialized stores	-4.2%	5.2%	2.7%	5.2%	2.7%
Fuel	6.1%	-0.3%	1.5%	1.5%	9.3%
IT and communication equipment	-4.4%	-2.5%	2.3%	1.4%	4.6%
Other household equipment	-8.9%	-3.8%	-3.3%	1.4%	4.3%
Cultural and recreation goods	2.1%	-2.7%	-3.8%	-0.2%	-0.6%
Pharmaceuticals and cosmetics	-1.2%	5.3%	5.2%	9.1%	7.0%
Textiles, clothing, footwear	-7.7%	-3.6%	-2.5%	-1.6%	2.1%
Sales via mail and internet	2.6%	12.8%	23.5%	17.8%	16.1%
Total, excl. vehicles, m/m sa	**-0.2%**	**-0.5%**	**0.4%**	**0.8%**	**0.1%**

Source: Czech stats office

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External trade surplus reaches CZK 14.3bn in August, stronger than expected

Czech Republic | Oct 07, 11:10

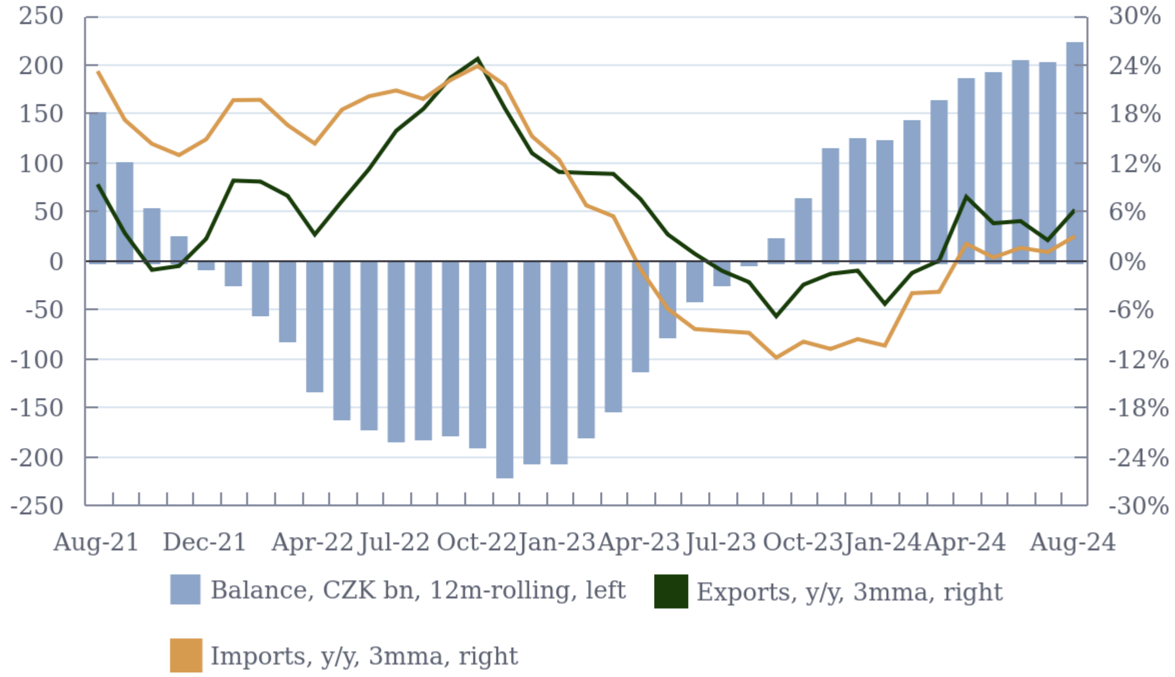
- **Markets expected a deficit of CZK 4.1bn**
- **The trade surplus reached CZK 165.9bn in January-August, up 2.6 times y/y**
- **Base effects related to the auto sector boosted motor vehicle exports**
- **However, performance elsewhere deteriorated**
- **We will see something similar in September, though low domestic demand would have produced some surpluses regardless**

The external trade surplus reached CZK 14.3bn in August (FOB/CIF), rising almost threefold in year-on-year terms, according to figures from the statistical office. The print was much stronger than the CZK 4.1bn deficit expected by markets. It brought the cumulative surplus to CZK 165.9bn in January-August, higher by 2.6 times in year-on-year terms. The 12m-rolling trade surplus thus hit CZK 224bn, its strongest level in a little over 3 years. In seasonally adjusted terms, the trade surplus reached CZK 27.4bn in August, higher by 2.6 times hen compared to July.

External trade

© EMW

Source | CSU



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The improvement in the trade balance in August was largely due to the auto sector, as motor vehicles accounted for more than 75% of the improvement. This is largely due to a base effect, as Toyota had major supply chain interruptions last summer, after a big parts supplier in Slovenia was heavily hit by floods. We will likely observe the same in September 2024, as Toyota did not recover completely until late September 2023. While there was some recovery elsewhere, it could be argued that the rest of the improvement was probably related to the auto sector in some capacity. In January-August, the trade surplus was also heavily impacted by the auto sector, which accounted for almost half of the improvement. However, there was also a strong contribution from manufactured articles, which is a category that includes military equipment and supplies, the production of which has been soaring after Russia invaded Ukraine in February 2022. There was also a strong increase in trade surpluses in the chemical and food sectors, while energy trade was the main factor pulling down trade surpluses.

Export growth eased to 11.5% y/y in August, slower by 1.4pps m/m. While motor vehicle exports soared, up by 25.9% y/y in August (from a 0.7% y/y drop in July), performance deteriorated everywhere else. This is in line with the base effect in the auto sector we refer to above, as non-automotive exports continued to report a worse performance. It strongly implies that once the base effect in the auto sector expires, we will see a much weaker export performance. In all fairness, exports rose by 9.2% m/m (sa), but we reckon this is due to a boost in the agricultural sector. Meanwhile, import growth eased faster, from 12.5% y/y in July to 5.2% y/y in August. The main reasons were chemicals and parts, whose imports performed much weaker. We would argue this is indicative of output prospects in the rest of 2024, and it is in line with reports of weaker purchasing activity by local producers. Moreover, oil & natural gas imports fell by 7.1% y/y in August after they rose by 9.4% y/y in July, but we can attribute this partially to lower global energy prices.

Overall, we are observing a temporary boost to trade surpluses caused by base effects that will completely expire in October. Nevertheless, we expect there would be some trade surplus regardless, given that domestic demand remains weak, and local producers are heavily dependent on imported raw materials and components. Thus, we will likely see trade surpluses remain solid throughout 2024, given that domestic recovery will be likely unimpressive this year.

External trade

	Aug-23	May-24	Jun-24	Jul-24	Aug-24
CZK mn					
Exports	332,827	384,149	389,506	358,072	371,090
Imports, CIF	339,290	371,841	358,656	363,667	356,788
Balance, FOB/CIF	**-6,463**	**12,308**	**30,850**	**-5,595**	**14,302**
12m rolling balance	-2,819	189,811	202,647	203,264	224,029
Change, y/y					
Exports	**-6.2%**	**0.1%**	**-3.2%**	**12.9%**	**11.5%**
Food and live animals	7.9%	8.6%	3.9%	24.7%	7.1%
Beverages and tobacco	1.4%	14.5%	5.6%	27.8%	23.3%
Crude materials	-28.3%	4.8%	5.9%	29.4%	11.6%
Mineral fuels, lubricants	-64.6%	-11.7%	-13.1%	-6.2%	-11.5%
Animal and vegetable oils	-21.5%	-18.2%	-20.8%	15.2%	-13.5%
Chemicals and related products	-9.0%	7.7%	4.7%	20.7%	6.6%
Manufactured goods by material	-12.3%	-1.7%	-4.9%	15.3%	1.4%
Machinery and transport equipment	2.5%	-1.5%	-5.0%	9.1%	16.3%
Manufactured articles	4.9%	4.0%	0.3%	18.4%	13.7%
Commodities not classified	-7.8%	14.3%	6.5%	23.5%	14.3%
Imports	**-11.7%**	**-0.6%**	**-6.7%**	**12.5%**	**5.2%**
Food and live animals	3.2%	12.6%	3.4%	23.3%	10.4%
Beverages and tobacco	-5.7%	0.9%	-6.5%	-11.9%	18.1%
Crude materials	-21.2%	6.8%	5.9%	7.9%	6.0%
Mineral fuels, lubricants	-49.4%	-8.4%	-9.3%	9.4%	-7.1%
Animal and vegetable oils	-26.2%	-11.0%	-14.4%	0.1%	-2.0%
Chemicals and related products	-12.5%	5.5%	-5.0%	23.2%	4.1%
Manufactured goods by material	-13.8%	-0.4%	-6.0%	18.4%	4.8%
Machinery and transport equipment	-0.8%	-3.1%	-9.2%	5.9%	5.2%
Manufactured articles	-2.7%	-0.5%	-6.0%	18.0%	10.4%
Commodities not classified	-58.6%	24.9%	43.5%	72.7%	32.5%

Source: CSU

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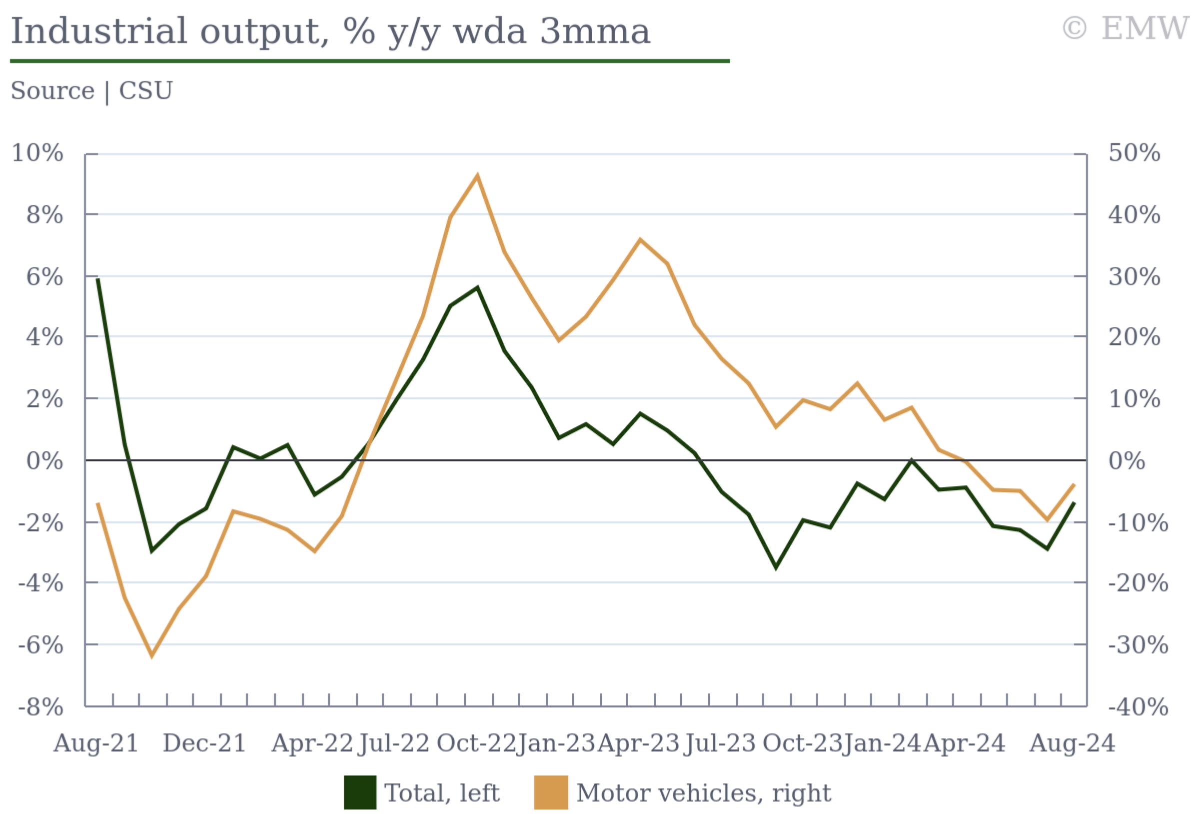
Industrial output rises by 1.5% y/y in August, above expectations

Czech Republic | Oct 07, 10:50

- **Markets expected a 1% y/y decline**
- **The auto sector drove the recovery, but it was largely due to a strong base effect**
- **Toyota had disruptions in its supply chains in August and September 2023, due to floods that hit a parts supplier in Slovenia**
- **Most other manufacturing sectors reported a deterioration, which is not encouraging for growth**
- **New orders rose by 9.9% y/y, but we see this as temporary**
- **Employment fell again by 1.9% y/y, while nominal wage growth eased to 4.4% y/y**
- **We will likely see a benign September print, but output will likely deteriorate in Q4 2024**

Industrial output rose by 1.5% y/y (wda) in August, reversing from a 1.9% y/y fall in July, according to figures from the statistical office. The print was visibly stronger than expectations, which put output on a

1% y/y decline. Output also rose by 1.8% m/m (sa), driven primarily by manufacturing, where the increase was as much as 2.1% m/m, the strongest since February.



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The big push came from manufacturing, where output rose by 2.1% y/y, ending three consecutive months of decline. The auto sector provided one of the main pushes, as it ended a 5-month period of decline and rose by 14.4% y/y. However, we argue that this is misleading, as there is a base effect in place related to Toyota, one of the three main passenger car manufacturers in the Czech Republic. Last year, Toyota's supply chain was hit by heavy floods in Slovenia, where one of its main parts suppliers is located. As a result, Toyota reported very low production numbers. To illustrate this, the normal monthly production of Toyota is about 19-20k units. The company produced only 4,365 units in August 2023 and 7,995 units in September 2023. The latter also implies we will see strong auto sector performance in year-on-year terms in September as well. However, we believe we don't need to spell it out, but once the base effect expires, auto performance will plunge again in year-on-year terms.

The latter is supported by the fact that only 5 out of the remaining 21 sectors reported an improvement, and most of them are not as significant. Those that deserve a mention are computers & electronics (up 7.9% y/y, faster by 1.7pps m/m), and non-metal minerals (up 2.9% y/y in August, reversing from a 2.6% y/y fall in July). Thus, if it weren't for the auto sector, we would probably see yet another deterioration in industrial performance. While manufacturing output rose at a solid rate in month-on-month terms, it was simply a return to the average from the past 12 months.

New industrial orders rose by an impressive 9.9% y/y (wda & sa) in August, reversing a 4.1% y/y fall in July. Improvement was across the board, but export orders rose by as much as 12% y/y, though they have been very volatile recently. It matches some improvement in business sentiment, though these days, it may simply mean that a bigger order has been received, which will nourish demand for a while. The matching improvement in domestic orders was smaller, as they rose by 5.9% y/y, though both order types decreased in year-on-year terms in July. Sales followed the general output trend, as they rose by 4.9% y/y in August, out of which export sales increased by 8.1% y/y. Yet, this is a normal development, as the auto sector exports more than 90% of its output.

If you want a longer perspective, it is better to look at employment numbers, which remain poor, as the number of employed in industry fell by 1.9% y/y in August, the same rate as in July. Employment in the sector has been falling since the middle of 2022, and there are no signs of easing thus far. After a spike in July, nominal wages eased their increase to 4.4% y/y in August. The average wage increase is currently 6.8% y/y in Q3 2024, which is the slowest since Q1 2022 (though by only a little). The main take here is that profit margins are narrowing, which doesn't allow industrial enterprises to boost wages at a faster rate. It is evidence that industrial producers do not expect any big boost to profits any time soon, so the spike in new orders is likely to remain temporary.

Overall, we are seeing mostly the impact of base effects, and we will observe the same in September. However, prospects for Q4 2024 are not so strong, given the poor signals still coming from Germany. We remind that the German PMI in September worsened to its weakest level in the past 12 months, which is not encouraging for Czech industrial producers that are tightly related to German demand. Thus, we expect that after the base effect in the auto sector expires, we will again see a decline in manufacturing output, with negative implications on overall economic recovery.

Industrial output

	Aug-23	May-24	Jun-24	Jul-24	Aug-24
Change, y/y wda					
Total	**-2.2%**	**-3.2%**	**-3.3%**	**-1.9%**	**1.5%**
Mining and quarrying	-17.4%	0.2%	-2.0%	-11.0%	-6.9%
Manufacturing	-0.9%	-4.0%	-3.9%	-2.1%	2.1%
Motor vehicles	6.1%	-6.8%	-6.9%	-16.2%	14.4%
Utilities	-10.2%	7.0%	4.2%	2.7%	-2.8%
Industrial orders	**-5.7%**	**1.0%**	**5.4%**	**-4.1%**	**9.9%**
Export	-4.9%	0.7%	6.8%	-5.7%	12.0%
Domestic	-6.9%	1.5%	2.9%	-1.1%	5.9%
Employment	-2.0%	-2.1%	-2.0%	-1.9%	-1.9%
Wages	9.0%	7.8%	3.2%	9.1%	4.4%
Output, m/m sa	**0.3%**	**-2.4%**	**0.8%**	**-0.8%**	**1.8%**

Source: Czech stats office

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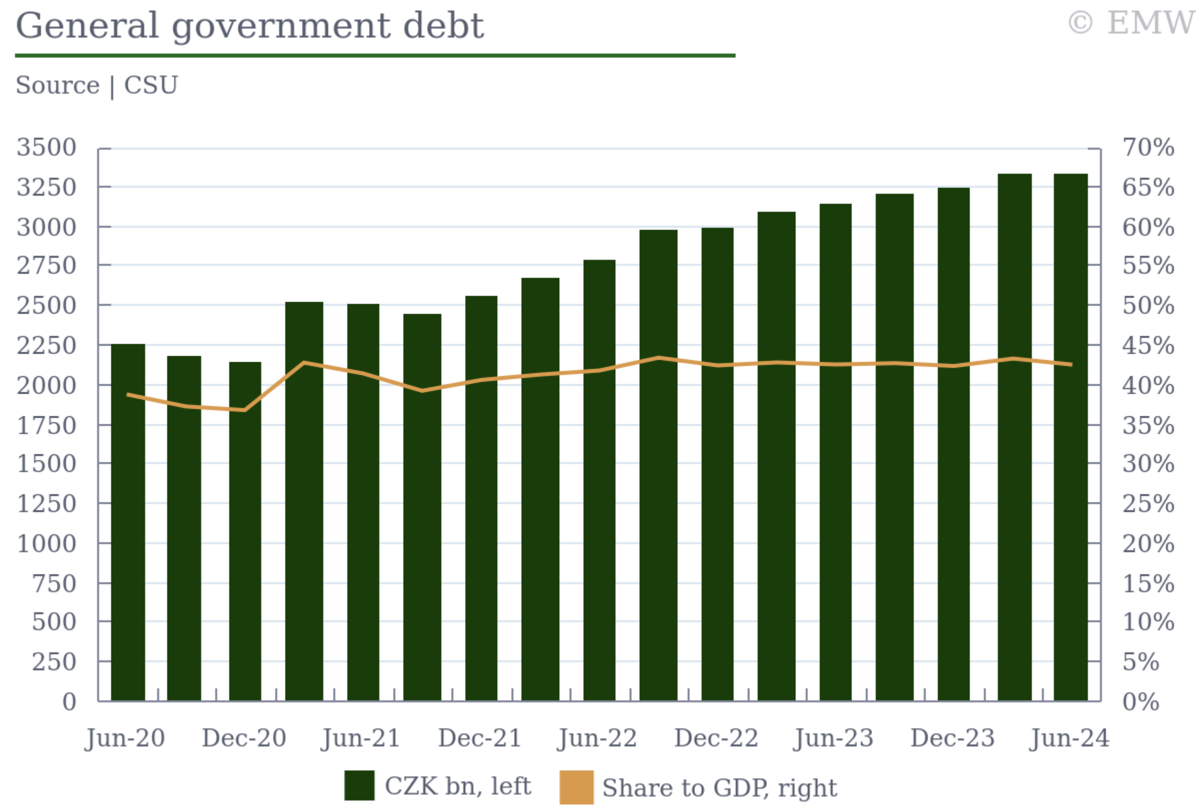
General government debt falls by CZK 17.5bn in Q2 2024 to CZK 3.32tn

Czech Republic | Oct 02, 11:21

- **Debt decline was mostly due to long-term securities**
- **Short-term debt remains low, at 3.4% of the total**

General government debt (Maastricht criteria) fell by CZK 17.5bn (0.5% q/q) in Q2 2024, down to CZK 3.32tn (42.6% of GDP) at the end of the quarter, according to figures from the finance ministry and the statistical office. The decline was primarily due to amortisation of government bonds, as well as lower debt issuance, in line with lower financing needs when compared to 2023. Thus, long-term securities fell by CZK 22.8bn in Q2 2024, and long-term debt was down by CZK 4.7bn. Short-term debt increased slightly, however, which brought the weight of short-term debt to 3.4% of the total at end-Q2. It is still a very low level, as the finance ministry has a clear preference for long-term debt instruments.



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In year-on-year terms, the debt stock increased by CZK 169.2bn (5.4% y/y). The increase was mostly due to long-term debt instruments, as well as long-term debt. The latter is mostly from the EU's SURE scheme, the last EUR 1bn tranche of which was delivered in Q4 2023. Additionally, short-term debt decreased strongly, down by CZK 43.7bn, which reflects the shift in strategy, as the finance ministry now relies on debt markets for liquidity, rather than short-term loans.

Overall, general government debt levels remain elevated, reflecting higher spending during the Covid-19 pandemic and the energy crisis. Debt levels will rise further, given the CZK 30bn that will be spent on repairing flood damage in 2024, so general government debt is anticipated to reach 44.1% of GDP at the end of 2024.

General government debt, CZK bn

	Q2 23	Q3 23	Q4 23	Q1 24	Q2 24
Total	**3,151**	**3,214**	**3,234**	**3,338**	**3,320**
Total, % of GDP	42.6%	42.8%	42.4%	43.4%	42.6%
Currency and deposits	24	25	31	28	30
Debt securities	2,856	2,923	2,943	3,050	3,035
Short-term	108	60	44	73	82
Long-term	2,748	2,864	2,899	2,976	2,954
Loans	271	266	260	260	255
Short-term	45	40	1	2	1
Long-term	226	226	258	258	253

Source: CSU, Ministry of Finance

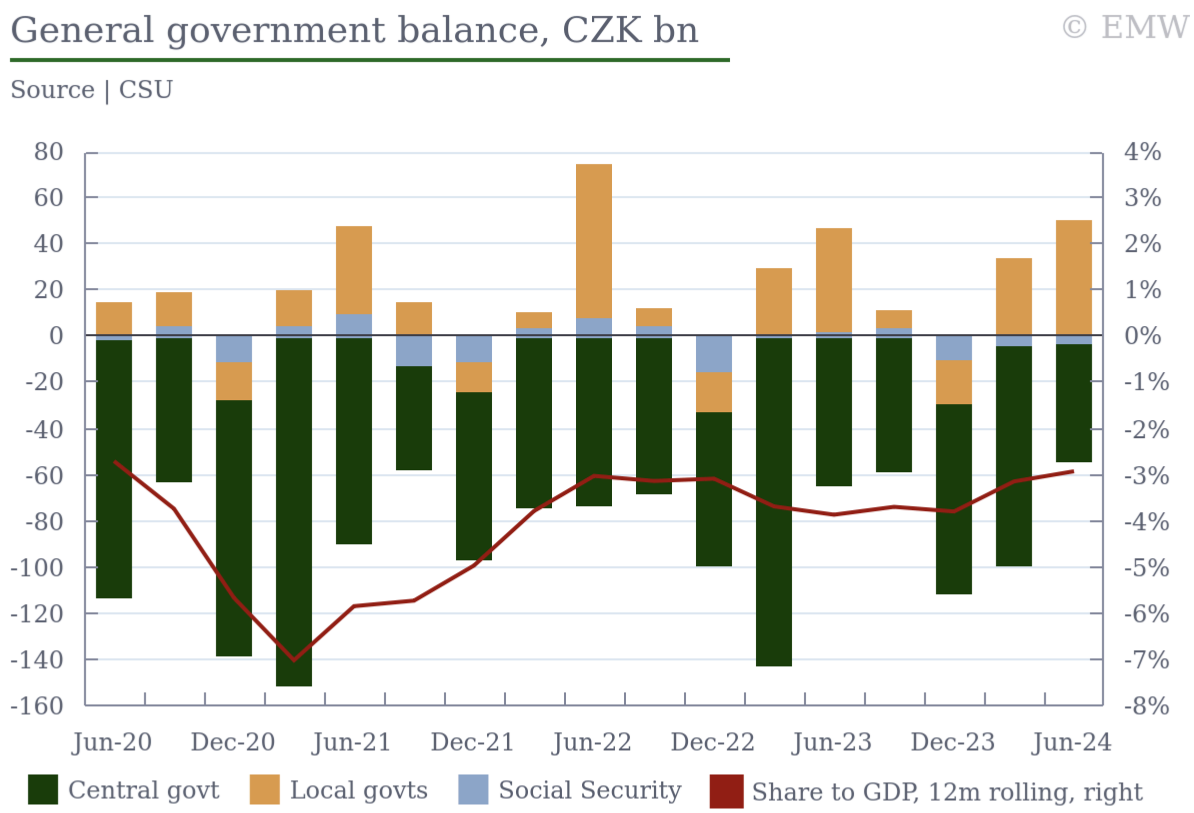
Ask the editor Link to source Back to contents

General government budget reports a deficit at 0.2% of GDP in Q2 2024

Czech Republic | Oct 02, 10:55

- **Annualised deficit reaches 2.9% of GDP at end-Q2, the lowest in 4 years**
- **Fiscal consolidation has produced results, visibly mostly in subsidies, which fell by 24.75 y/y in H1 2024**
- **The biggest improvement was at central government level, local government budgets improved strongly as well**
- **Data confirms claim that budget performance was in line with the plan in H1**
- **Extraordinary expenses caused by floods to bring the general government deficit to 2.8% of GDP in 2024**

The general government budget reported a deficit of CZK 3.5bn (0.2% of GDP) in Q2 2024, according to figures from the finance ministry and the statistical office. In 4q-rolling terms, the general government deficit eased to 2.9% of GDP at end-Q2, its lowest level in 4 years. Thus, this government is the first that has managed to bring down general government deficits downwards after the pandemic and the energy crisis.



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Revenues rose by 5.6% y/y in Q2 2024 and by 7.1% y/y in H1 2024. In both periods, social contributions were the primary growth driver, as they increased by 8.4% y/y in Q2 and 8.6% y/y in H1. There was also a strong impact from income taxes, which is mostly due to windfall tax, benefiting from a base effect. We remind that in 2023, windfall tax was collected only in September and December, while in 2024, it has been collected at the end of each quarter. Thus, windfall tax data will be comparable only as of Q3 2024, and until then, the base from 2023 will be visibly lower. Indirect taxes saw an 8.2% y/y increase in Q2 2024, likely due to the expiration of base effects related to energy and other commodity exports. Their increase was a solid 4.9% y/y in H1 2024, but VAT proceeds rose by only 1.8% y/y, reflecting a slower-than-expected recovery of the economy. There was also a strong downward base related to other property income, mostly related to the record dividend payout by CEZ in 2023, which did not repeat in 2024 and led to a 40.2% y/y slump of non-interest property income.

On the expenditure side, spending rose by 3.8% y/y in Q2 2024 and by 2.7% y/y in H1 2024. Social expenses were again the main increase in spending, rising by 5.3% y/y in Q2 and 5.8% y/y in H1. Compensation of employees increased by 4.1% y/y in H1 2024, at relatively uniform rates throughout the year. This includes pay rise in education, which is normally not reflected in state budget execution, as most education facilities are run by local governments. Subsidies decreased by 24.7% y/y in H1 2024, in line with the expiry of energy support schemes in 2023.

By government level, the biggest improvement in the general government balance came from the central government, whose deficit reached CZK 50.8bn (2.5% of GDP) in Q2 2024, the lowest quarterly deficit since before the Covid-19 pandemic. Annualised, the central government deficit eased to 3.7% of GDP at end-Q2, the lowest level in 4 years. Local government budgets continued to perform well, though they reflect a higher share of nationally collected taxes, which will increase further until 2027. Thus, local government budgets had an annualised surplus at 0.9% of GDP at end-Q2, which is what we have been seeing since 2021. There was some increase in the deficit of social security funds, as unemployment is a bit higher than in 2023.

All in all, it appears that general government budget performance was in line with the plan in H1 2024. We expect to see the same in Q3 2024, as flood-related expenses will not be made before Q4 2024. We remind that according to the revised 2024 budget law, the general government deficit target is now 2.8% of GDP in 2024, up from 2.5% of GDP initially targeted.

General government balance

	Q2 23	Q3 23	Q4 23	Q1 24	Q2 24
CZK mn					
Total	**-17,519**	**-47,284**	**-110,775**	**-65,253**	**-3,513**
Central government	-64,424	-58,290	-82,053	-95,030	-50,848
Local government	45,723	7,531	-19,108	33,354	50,484
Social security funds	1,182	3,475	-9,614	-3,577	-3,149
% of GDP					
Total	**-0.9%**	**-2.4%**	**-5.6%**	**-3.5%**	**-0.2%**
Central government	-3.3%	-3.0%	-4.1%	-5.1%	-2.5%
Local government	2.4%	0.4%	-1.0%	1.8%	2.5%
Social security funds	0.1%	0.2%	-0.5%	-0.2%	-0.2%
Total, 12m rolling	**-3.9%**	**-3.7%**	**-3.8%**	**-3.1%**	**-2.9%**

Source: CSU

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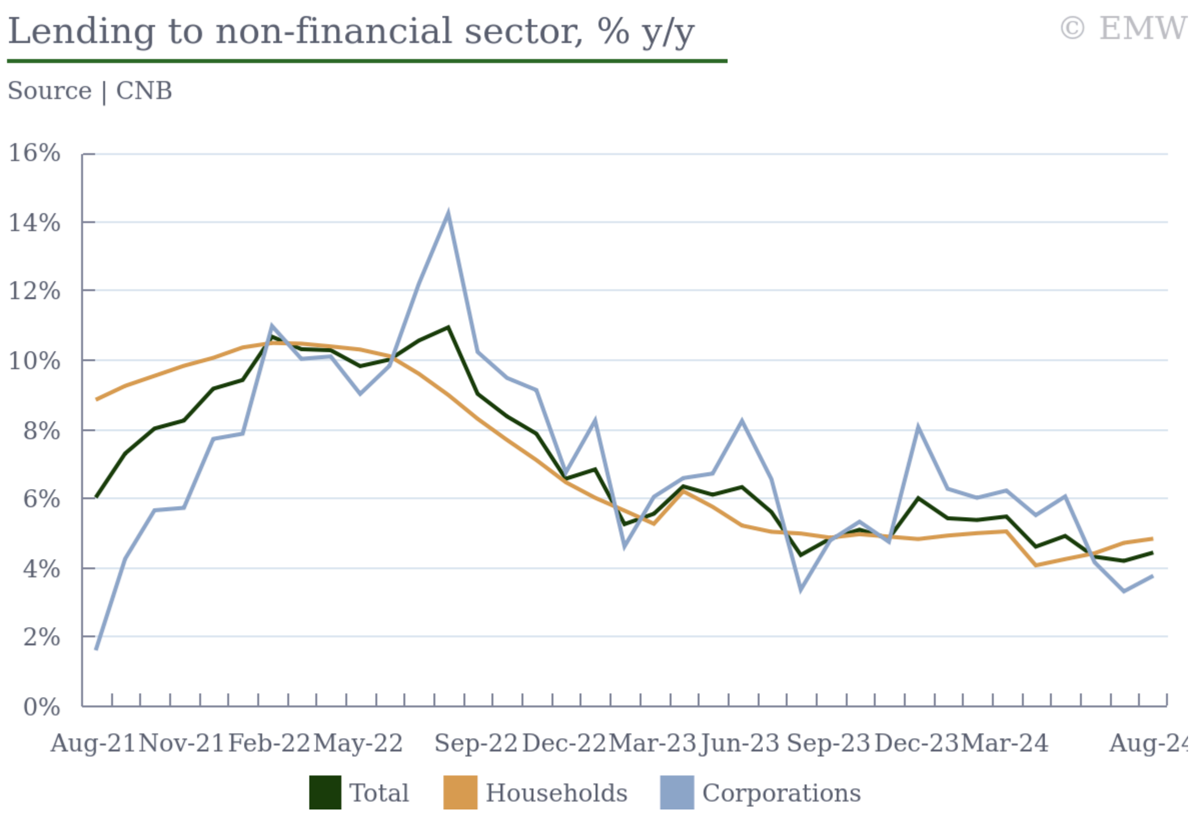
Lending to private sector picks up growth to 4.5% y/y in August

Czech Republic | Sep 30, 12:03

- **Long-term corporate loans drove the increase, reflecting lower borrowing costs**
- **Housing loans kept recovering, though lending rates are falling slower**
- **M3 growth eased a bit, remains moderately above projected nominal GDP growth in Q3**

Lending to the private sector picked up growth to 4.5% y/y in August, up from 4.2% y/y in July, according to figures from the CNB. Corporate lending was again the source of stronger growth, as loans to non-financial corporations rose by 3.8% y/y in August, faster by 0.4pps m/m. As borrowing costs have continued to decline, there was a boost in long-term loans (over 5 years), which increased by 4.7% y/y, their fastest growth over the past 5 months. To illustrate, borrowing costs fell by 235bps over the past 12 months, in line with the monetary easing cycle currently in place. Corporate loans denominated in foreign currency remained roughly around half of all new loans, at 52% in August, which indicates that EUR-denominated loans, which are most of fx loans, are still more lucrative.



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Lending to households accelerated its growth as well, up by 4.9% y/y in August, faster by 0.1pps m/m. Housing loans again led the stronger increase, rising at their strongest rate in the past 5 months. Borrowing costs on housing loans were lower by 51bps y/y, while rates on pure new mortgage loans (i.e. excluding refinanced and restructured loans) were down 80bps to 5.07%, close to what was predicted by the Czech Bank Association's Hypomonitor survey. Banks remain relatively cautious about housing loans, as despite the cumulative 275bps of monetary easing since December 2023, housing loan rates have decreased much slower. Consumer loans kept rising fast, up by 9% y/y in August, though they have been rising by at least 8% y/y since the beginning of 2022. Still, this has been brought up during CNB board meetings on financial stability as a potential risk, even though we have not seen any massive deterioration in household loans recently. There may be some need to observe housing loans closely, though, as pure new housing loans rose 2.2 times in year-on-year terms, even though the base is a bit low.

Broad money supply (M3) eased its increase to 5.7% y/y in August, in nominal terms, though M3 growth remains a bit higher than projected nominal GDP growth in Q3 2024 (4.5% y/y, according to the CNB's forecast). In all fairness, deposits are still rising at a strong rate, given that real interest rates are still positive, so it may not be a big reason for concern. M1 rose by 6.5% y/y, or faster than M3, which reflects some recovery in consumption. In real terms, M3 increased by 3.4% y/y, slower by 0.4pps m/m, while M1 was higher by 4.2% y/y, the same rate as in July.

Monetary developments

	Aug-23	May-24	Jun-24	Jul-24	Aug-24
Change, y/y					
Loans to private sector	**4.4%**	**5.0%**	**4.4%**	**4.2%**	**4.5%**
Non-financial corporations	3.4%	6.1%	4.2%	3.4%	3.8%
Households	5.0%	4.3%	4.4%	4.8%	4.9%

consumer	8.9%	8.5%	8.5%	8.9%	9.0%
housing	4.5%	3.4%	3.6%	3.9%	4.0%
other	3.7%	5.3%	5.5%	5.6%	5.5%
Pure new housing loans	35.8%	86.7%	69.6%	107.4%	122.0%
M1	1.3%	5.4%	6.0%	6.4%	6.5%
M3	9.6%	5.8%	5.3%	6.0%	5.7%
Interest rates, new business					
Households	**6.82%**	**6.11%**	**6.07%**	**6.16%**	**5.89%**
Consumer	9.57%	8.86%	8.90%	9.02%	8.81%
Housing	5.51%	4.99%	5.00%	5.03%	5.00%
Other	6.50%	5.56%	5.54%	5.65%	5.50%
Non-financial corporations	**8.51%**	**6.91%**	**6.58%**	**6.42%**	**6.16%**
Renegotiated housing loans, % of total	57.7%	50.9%	51.8%	54.1%	53.9%

Source: CNB

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Gross external debt rises by EUR 1.1bn in Q2 2024 to EUR 195.4bn

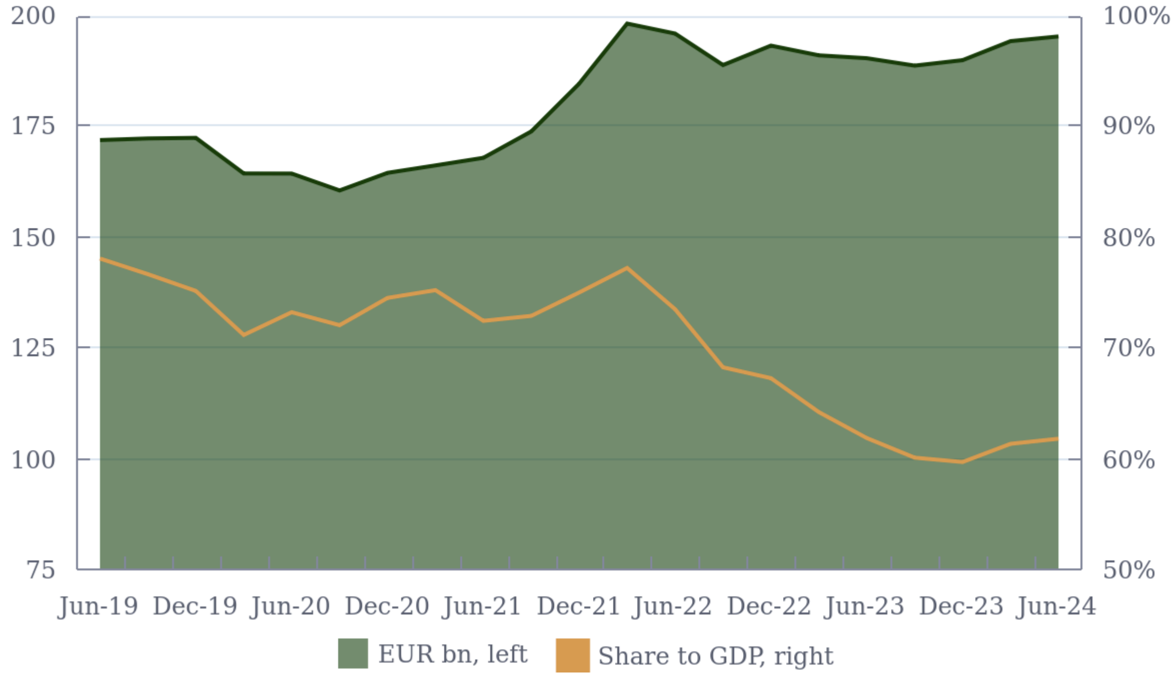
Czech Republic | Sep 20, 11:29

- **External debt reached 61.9% of GDP at end-Q2**
- **Short-term debt as 50.6% of the total, but half of these were short-term deposits**
- **External debt increased mostly due to bank debt and trade credits in Q2**
- **No immediate risk to debt service is observed**

Gross external debt rose by EUR 1.1bn (0.5% q/q) in Q2 2024, adding up to CZK 195.4bn (61.9% of GDP) at the end of the quarter, according to figures from the CNB. In year-on-year terms, the external debt stock rose by EUR 4.9bn (2.6%). As usual, the share of short-term debt was considerable, at 50.6% of the total, though it was largely due to short-term deposits of non-residents, which accounted for 24.8% of headline debt. Specifically, banks and non-financial corporations had 31.2% of their external debt being short-term, lower by 5.6pps y/y, after excluding non-resident deposits. Compared to peers in the AA rating group, external liabilities are relatively low. Moreover, only 11.6% of medium- and long-term external debt is due over the next 12 months, while 72.5% of external debt is due in more than 2 years, so no major immediate risks are present.

Gross external debt

Source | CNB



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In Q2 2024, the external debt stock rose mostly due to short-term securities issued by banks, as well as due to trade credits and non-resident deposits. Trade credits were mostly for direct investment purposes, though, so they will surely pay off. Both the CNB and the government reported a decline in their debt stock, though in the case of the CNB, it was almost entirely due to lower non-resident deposits. Thus, there was nothing particularly extraordinary, as the chapters where the significant changes took place are typically volatile. Regarding the past 4 quarters, the debt increase was mostly due to banks and non-financial corporations, both through long-term debt securities. There was also a sizeable increase in long-term trade credits, again primarily for investment purposes. Meanwhile, the government saw a decline in external debt, but it was mostly due to discontinuing the practice of drawing short-term loans for liquidity purposes, as the finance ministry currently uses local debt markets for that purpose.

Overall, external indicators remain stable, and debt levels are manageable. There hasn't been any big expansion of indebtedness, even though the corporate sector is looking into cheaper financing abroad. Lending statistics shows that about half of corporate loans are in euro, which is mostly due to lower borrowing costs. Yet, it hasn't led to a debt explosion, and the maturity of debt liabilities is not posing any immediate risk.

Gross external debt, EUR mn

	Q2 23	Q3 23	Q4 23	Q1 24	Q2 24
Total	**190,501**	**188,833**	**190,063**	**194,347**	**195,409**
Short-term	100,920	98,868	97,044	97,475	98,925
Long-term	89,581	89,966	93,019	96,872	96,484
by instruments					
Currency and deposits	51,328	51,812	57,254	57,910	57,066
Debt securities	51,626	52,005	48,015	46,778	48,759
Loans	55,454	51,430	52,738	54,210	52,894
Trade credits and advances	24,288	25,731	24,465	27,554	28,980
Other liabilities	4,284	4,304	4,107	4,377	4,183

by debtor					
Central Bank	9,852	11,095	8,460	9,706	7,261
Banks	63,075	62,829	65,705	63,906	67,686
General government	33,778	33,662	32,746	32,660	31,802
Other sectors	83,796	81,247	83,152	88,075	88,659
Total, % of GDP	**61.9%**	**60.2%**	**59.8%**	**61.4%**	**61.9%**

Source: CNB

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CA deficit reaches CZK 13.7bn in July, better than expected

Czech Republic | Sep 13, 11:36

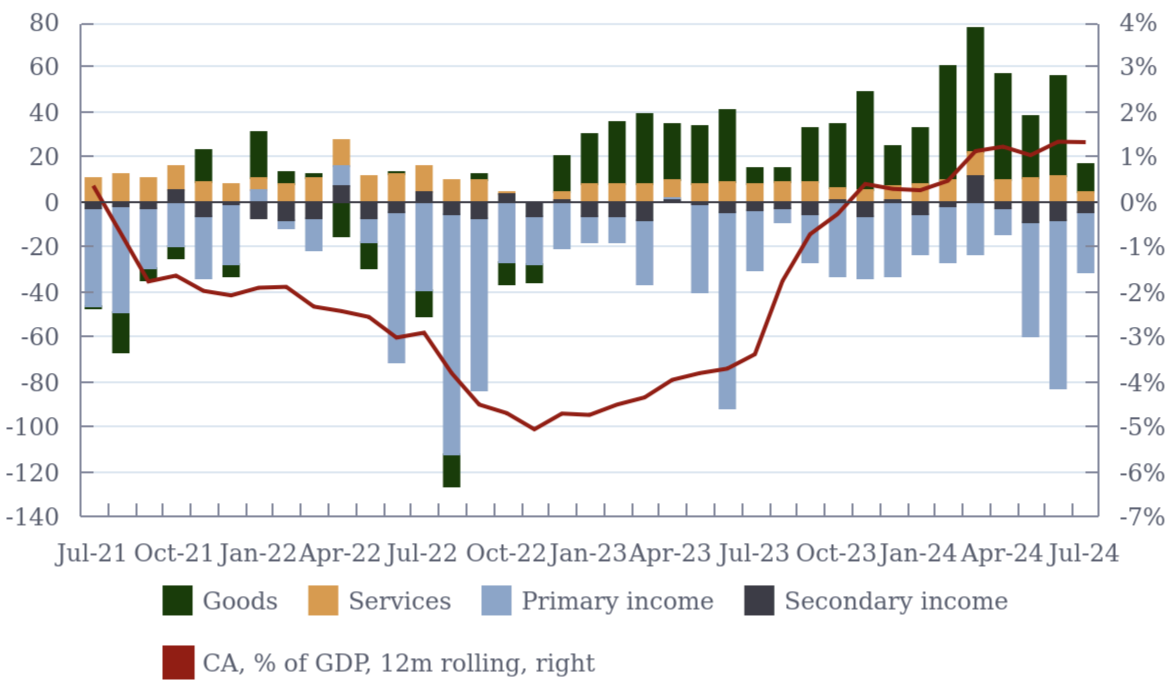
- **Markets expected a deficit of CZK 20.7bn**
- **The CA surplus reached CZK 82.8bn in January-July, while the 12m-rolling surplus was 1.4% of GDP at end-July**
- **Not a lot was seen in the CA balance in July, goods' trade continued to expand its surplus**
- **The January-July CA surplus expanded mostly due to goods' trade, with some lingering effects related to energy prices**
- **Net financial flows were positive in July but negative in January-July, the latter driven by gains in official reserves**
- **We expect a CA surplus above 1% of GDP in 2024, still a decent level in 2025**

The current account reported a deficit of CZK 13.7bn in July, lower by 3.6% y/y, according to figures from the CNB. The print was better than anticipated, as markets projected a deficit of CZK 20.7bn. The CA balance was still at a CZK 82.8bn surplus in January-July, reversing from a deficit of CZK 0.1bn last year. The 12m-rolling CA balance saw a surplus of CZK 106.7bn (1.4% of GDP) at end-July, its strongest performance since late 2020.

Current account structure, CZK bn

© EMW

Source | CNB



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Given the small change in the CA balance in year-on-year terms in August, there were no major developments in the various components of the current account, either. Goods' trade saw a higher surplus by 72.9% y/y, but it was still a relatively modestly one, at CZK 11.9bn. It reflects low external demand, as Czech manufacturers are heavily dependent on imported commodities and parts, so when external demand is weak, imports also fall sharply. PMI surveys have indicated that input purchases have consistently decreased in 2024, as producers are still mostly relying on inventories for production. Service flows had a downward impact, lower by 41.8% y/y, which we attribute mostly to transportation flows, which have decreased after external demand has remained low. Primary income flows were unchanged in year-on-year terms, and secondary income flows had a negligible impact.

The situation was a bit different in cumulative terms, as the big improvement in the CA balance was supported by goods' trade, whose surplus was up 54.3% y/y. We should note that early in 2024, there was still a favourable base effect related to energy goods, which kept export growth at 3.5% y/y, while imports fell by 0.1% y/y. This will change later in 2024, but we will still have some favourable impact, keeping the goods' trade surplus stronger than usual. Primary income flows remained negative, rising by 12.4% y/y, which we attribute to strong dividend payouts and profit repatriation.

Net financial flows were positive in July, at CZK 16.4bn, though lower by 34.6% y/y. Meanwhile, financial flows remained heavily negative in January-July, higher by 2.3 times in year-on-year terms, which was in line with the strong CA surplus reported. The smaller amount of net financial inflows in July was due primarily to official reserves, which increased steadily. This likely reflects the higher price of gold, as the CNB expanded the weight of its monetary gold more than twice over the past year. On a positive note, net direct investment flows turned positive in July, though they covered only about 37% of the CA gap. In January-July, net financial flows turned increasingly negative due to official reserves, mitigated by an increase in non-resident deposits in local banks, but only partially. Even though the CNB has been selling about EUR 300mn monthly in 2024, as part of its programme to unload earnings on reserve management, it has been earning a lot more. In all fairness, higher gold prices were not the only factor, as a weaker CZK is usually bringing higher profitability from reserve management, and the CZK has lost some value after monetary easing started in December 2023.

Overall, the balance of payments remains stable, and we will likely observe a CA surplus above 1% of GDP in 2024. This is highly reliant on weak external demand, and as soon as the Czech Republic's main trade partners start recovering, we will see a correction in external balances. Commodity and energy prices also have an impact, and oil prices have decreased recently to a 3-year low, which also has an impact on external balances. Given our scepticism about Germany's recovery in 2025, we expect that the CA surplus will remain solid, possibly around 0.5% of GDP, as we still expect some recovery, just not as strong as currently implied.

Balance of payments, CZK bn

	July			January-July		
	2023	2024	Change	2023	2024	Change
Current account	**-14.3**	**-13.7**	**0.5**	**-0.1**	**82.8**	**82.9**
Goods	6.9	11.9	5.0	170.6	263.3	92.7
Exports	310.1	349.9	39.8	2,560.4	2,649.7	89.3
Imports	303.3	338.0	34.8	2,389.7	2,386.4	-3.3
Services	8.7	5.1	-3.6	58.9	66.2	7.3
Primary income	-26.8	-26.8	0.0	-203.5	-228.6	-25.1
Secondary income	-3.1	-3.9	-0.9	-26.2	-18.1	8.1
Capital account	**1.9**	**4.6**	**2.7**	**64.7**	**55.6**	**-9.1**
Financial account	**-25.1**	**-16.4**	**8.7**	**57.9**	**134.6**	**76.7**
Direct investment	21.2	-5.1	-26.3	-21.5	-18.5	3.0

Portfolio investment	-19.0	-28.0	-9.0	-20.0	23.7	43.8
Financial derivatives	-3.4	-5.6	-2.2	14.4	-27.8	-42.2
Other investment	-1.6	8.7	10.3	181.8	117.8	-64.0
Reserve assets	-22.2	13.7	35.9	-96.8	39.4	136.1
Net errors and omissions	**-12.8**	**-7.3**	**5.5**	**-6.6**	**-3.8**	**2.8**

Source: CNB

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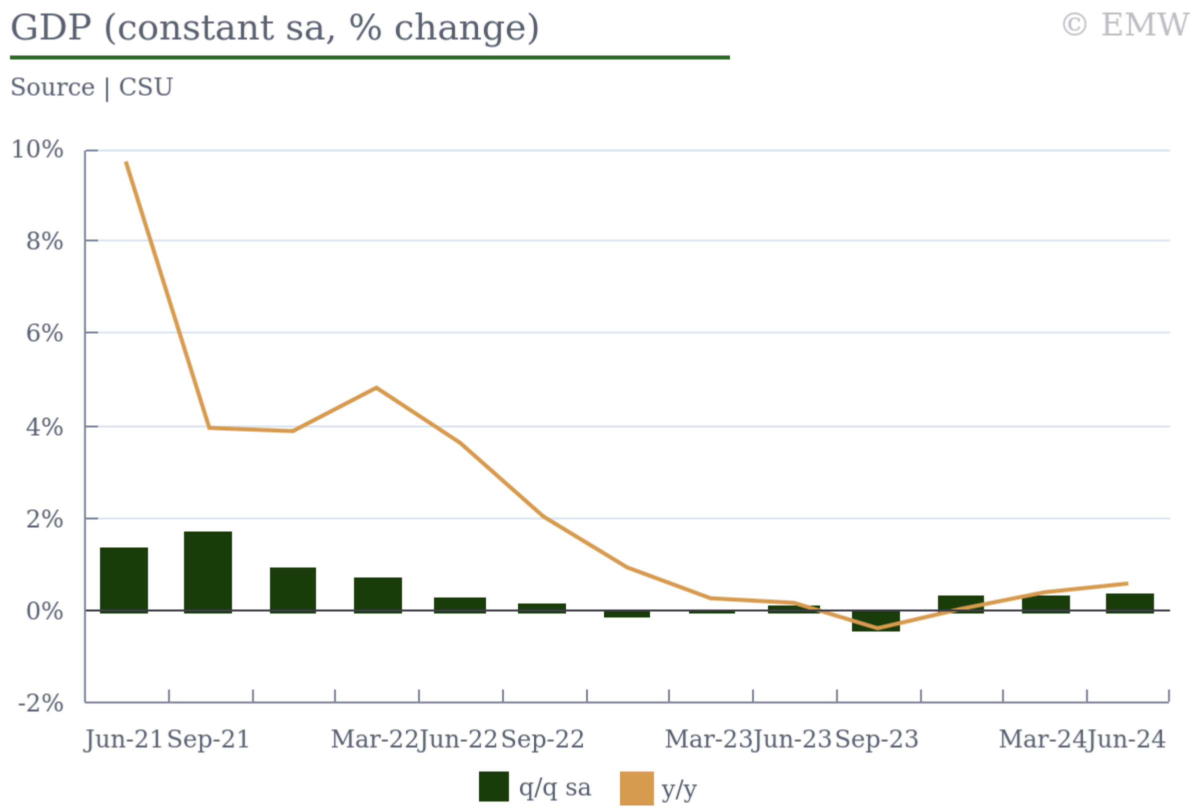
GDP growth revised upwards to 0.6% y/y in Q2 2024

Czech Republic | Aug 30, 10:46

- **Quarter-on-quarter GDP growth left unchanged at 0.3% q/q**
- **Household consumption growth weakened, exerting a downward impact on GDP growth dynamics**
- **Inventories and, to a lesser extent, capital formation, were behind a stronger GDP growth in Q2**
- **Expectedly, net exports weakened, in line with poor external demand**
- **Slow recovery in household spending justifies the more aggressive approach of the CNB to rate cuts in H1 2024**

GDP growth was revised upwards, from 0.4% y/y to 0.6% y/y in Q2 2024, according to the second release of national accounts from the statistical office. There was no major change in quarter-on-quarter numbers, as the GDP is still estimated to have increased by 0.3% q/q (sa). This puts the revised year-on-year print exactly in line with the CNB's latest staff forecast, while the finance ministry used the flash estimate provided by the statistical office a month ago. There is still some discrepancy with the CNB's quarter-on-quarter projection, as the CNB expected GDP growth at 0.4% q/q (sa). Additionally, the statistical office revised GDP growth figures slightly upwards in Q1 2024, from 0.3% y/y to 0.4% y/y.



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Importantly, the breakdown shows that it was inventories that led to the slight acceleration of GDP growth in Q2 2024. The impact of inventories remained negative, at -2.2pps in Q2 204, but it was milder by 0.7pps q/q. Moreover, gross fixed capital formation recovered from a 0.1% y/y fall in Q1 to a 0.7% y/y increase in Q2. Meanwhile, household consumption had a downward impact on growth dynamics, as its increase eased from 1.7% y/y in Q1 to 1.0% y/y in Q2. It reflects an unconvincing recovery in household spending, as while there was an improvement, it was not reported in major purchases. In all fairness, government spending mitigated that impact, as it rose by 4.3% y/y in Q2 2024, faster by 1.1pss q/q. Still, final consumption had a downward impact on growth dynamics, which reflects lower-than-expected inflation in the quarter.

As expected, net exports eased their positive contribution to GDP growth, from +1.9pps in Q1 to +1.3pps in Q2. It reflects the expiration of favourable base effects related to energy and other commodity prices, as well as growing obstacles to global trade. This is likely to continue, so the odds are there will be a lid on GDP growth in the coming quarters.

On the supply side, the sectors that drove faster growth were financial and professional services, both seeing a solid improvement in growth rates when compared to the previous quarter. Real estate, trade & transportation, and construction also had a modest upward impact. Meanwhile, manufacturing expectedly did poorly, as its output growth eased to its softest rate in the past 9 quarters, at 3.9% y/y in Q2 2024. The auto sector has been particularly struggling, given weak demand from major markets like Germany and France.

Weaker recovery in household spending justifies the CNB's aggressive rate cuts in H1 2024

Our conclusions about growth in Q2 2024 are that while household consumption remains a major factor, it did worse than anticipated. It appears that wages did not rise as quickly as anticipated, though we will only get confirmation for that next week, when the Q2 print is published on Sep 3. Importantly, easing household spending was likely behind a weaker-than-expected inflation in Q2 2024. The July CPI print was slightly above the 2% y/y expected in Q3 2024, but the deviation is marginal so far, which means that we may still observe a more solid recovery in household consumption this quarter. As far as the first half of the year is concerned, however, the numbers justify the more aggressive approach of the CNB board towards monetary easing.

Regarding the rest of the year, a lot will depend on whether recovery will speed up. Quarter-on-quarter growth has remained around 0.3% since Q4 2023, and it that is still the case, it implies GDP growth of around 0.9-1% in 2024. This will be slightly below official expectations, as the CNB expects GDP growth at 1.2%, and the finance ministry - at 1.1%. We reckon external demand will be instrumental, and given signals we have seen thus far, we expect that GDP growth may remain around 0.3% q/q in Q3 2024 at least, which means a year-on-year growth of 1.3% y/y.

GDP by components, % y/y, sa

	Q2 23	Q3 23	Q4 23	Q1 24	Q2 24
GDP	**0.2%**	**-0.4%**	**0.0%**	**0.4%**	**0.6%**
Final consumption	-1.4%	-0.9%	0.8%	2.2%	2.0%
Households	-3.3%	-2.9%	-0.5%	1.7%	1.0%
Government	3.0%	3.8%	3.9%	3.2%	4.3%
Gross capital formation	-6.3%	-3.8%	-14.2%	-9.9%	-7.2%
o/w: Gross fixed capital formation	3.6%	2.4%	2.2%	-0.1%	0.7%
Exports	5.3%	-0.2%	0.9%	-0.1%	0.4%
Imports	1.0%	-2.2%	-4.6%	-2.9%	-1.5%
GDP, % q/q	**0.14%**	**-0.38%**	**0.28%**	**0.37%**	**0.33%**

Gross value added	**10.7%**	**7.6%**	**6.1%**	**3.5%**	**4.4%**
Agriculture	-11.7%	-20.3%	-21.8%	-19.8%	-15.2%
Industry	16.2%	10.2%	10.0%	5.2%	4.5%
o/w: Manufacturing	15.6%	9.4%	8.1%	6.7%	3.9%
Construction	9.7%	5.7%	2.2%	-0.4%	0.9%
Trade, transportation, accommodation, food	13.4%	12.4%	8.1%	4.2%	4.7%
Information & communication	11.5%	9.5%	7.5%	5.0%	7.3%
Financial and insurance activities	1.6%	6.5%	-0.1%	4.3%	7.3%
Real estate activities	7.5%	4.8%	4.9%	2.7%	3.9%
Professional services	7.1%	3.9%	4.9%	3.5%	6.6%
Public administration, education, health	8.1%	6.6%	4.9%	4.0%	4.9%
Other services	9.1%	2.8%	6.8%	4.7%	3.2%

Source: Czech stats office

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