

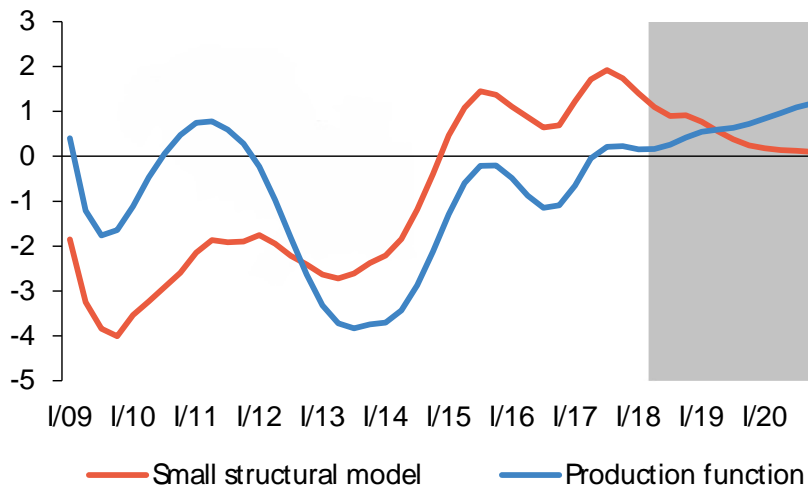
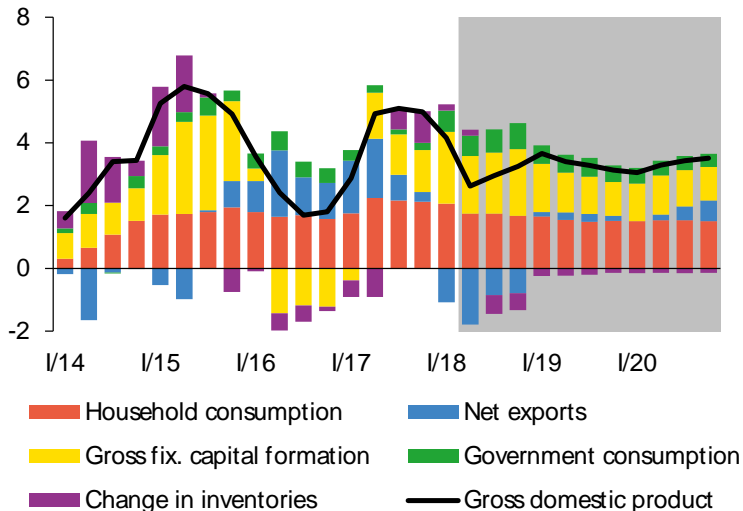
# Economic growth prospects in the Czech Republic

Petr Král

Deputy Executive Director, Monetary Department

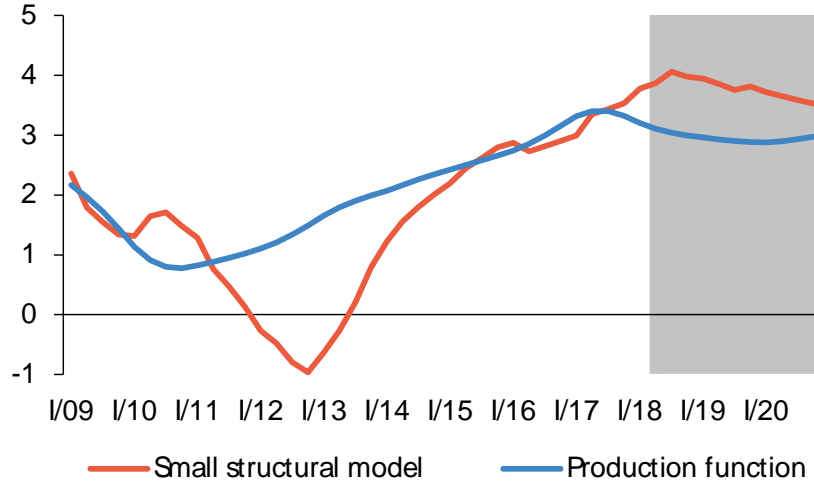
Czech National Bank

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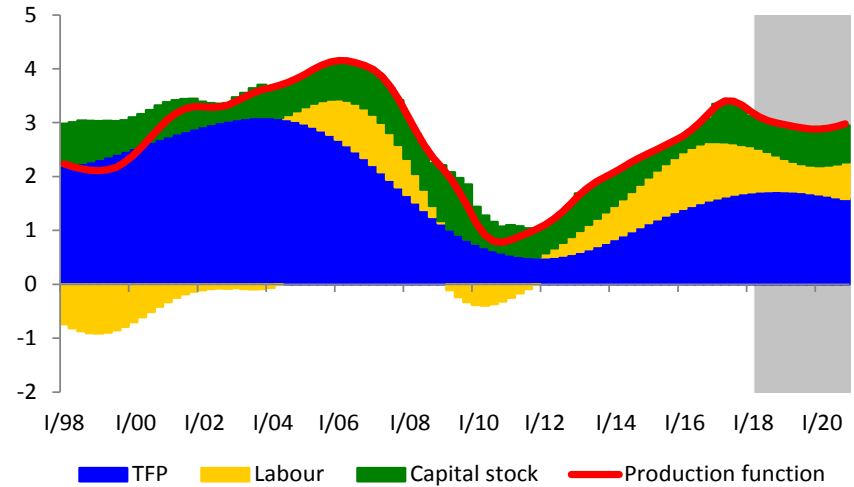


- Consumption and investment will contribute to ongoing swift GDP growth over the entire forecast horizon; the contribution of net exports will temporarily be negative this year.
- According to the small structural model the positive output gap will close gradually. This is consistent with a still tight labour market situation and strong domestic – and to a lesser extent external – demand. By contrast, the production function suggests a less open output gap at present but a steady widening of the gap over the entire horizon.

## Potential output growth

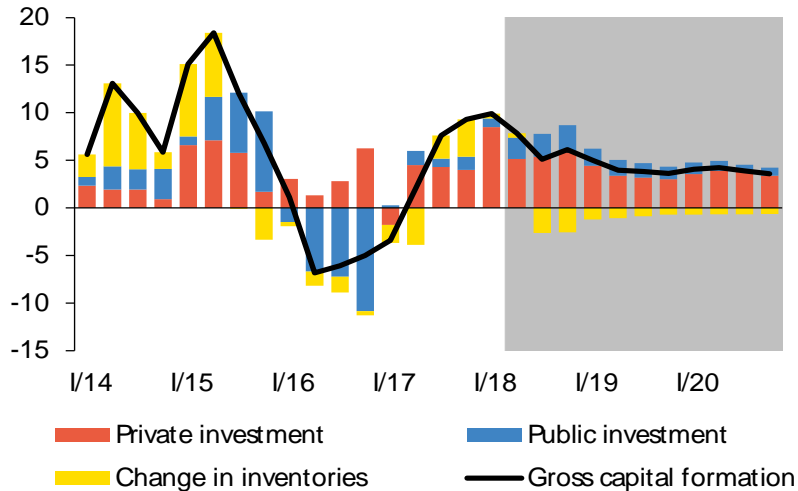


## Potential output growth contributions

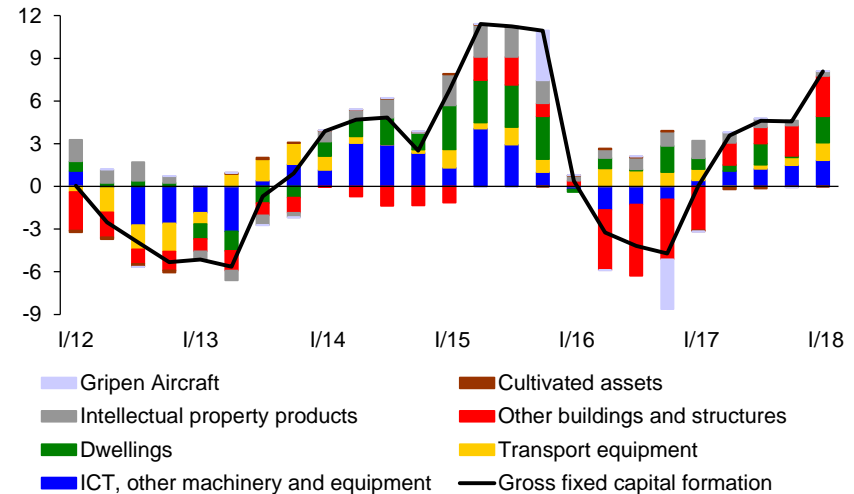


- According to the small structural model, potential output growth accelerated to 4% but will gradually slow; according to the production function, it will fluctuate around 3%.
- Capital stock increases have been generating a relatively stable contribution to  $Y^*$  growth when identified by a standard Cobb-Douglas production function. Variations in  $\Delta Y^*$  are rather caused (explained) by TFP and labour force contributions.

(% y-o-y; contributions in pp)

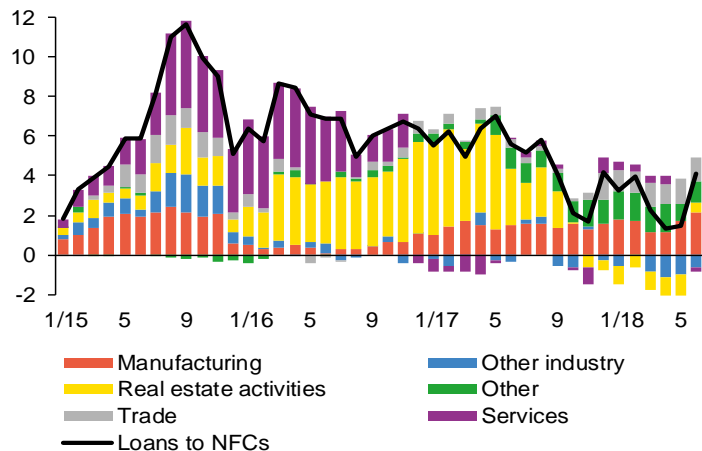


(% y-o-y; contributions in pp)



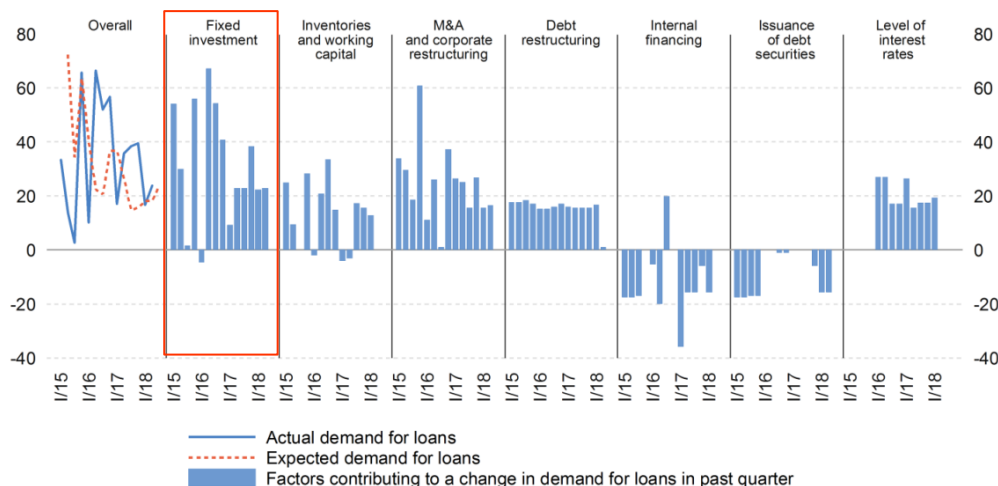
- Gross capital formation will rise due to continued growth in private investment (mainly by NFCs) and government investment partly co-financed from EU funds.
- Solid growth in external demand combined with a tight domestic labour market will spur additional investment in the business sector, fostering an increase in labour efficiency (productivity gains).
- Investment in buildings, dwellings and machinery dominates the structure. This also reflects firms' efforts to streamline production amid labour market constraints.

## Loans to non-financial corporations (contributions in pp)



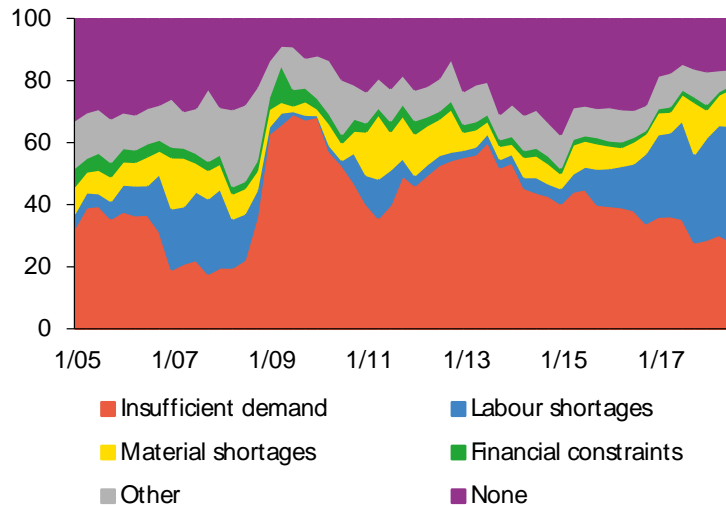
Note: Other comprises transport, construction and agriculture.

## Changes in NFC demand for loans based on BLS (net percentages, positive value = demand growth, negative value = demand decrease)

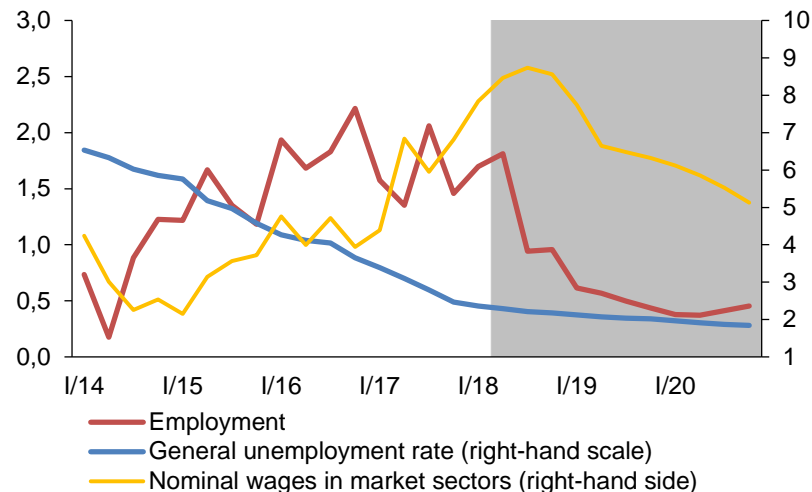


- The growth in loans to NFCs is mainly due to increasing loans to manufacturing, construction and transport.
- As indicated in our Bank Lending Survey, fixed investment is a regular and solid source of perceived demand for NFC loans.

## Barriers to growth in industry (percentages)



(annual percentage changes in employment;  
general unemployment rate in percentages; s.a.)



- Labour shortages continue to be the most important constraint on the production growth of industrial corporations.
- Total employment will rise at a substantially slower pace than before, while the decline in the unemployment rate will moderate.
- The exhausted labour market has led to accelerated nominal wage growth.

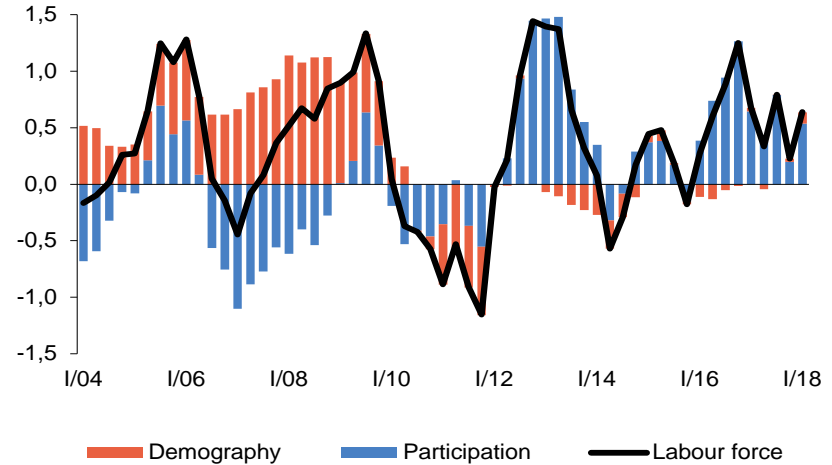
## Employment and the labour force

(annual percentage change, age 15 years or more)

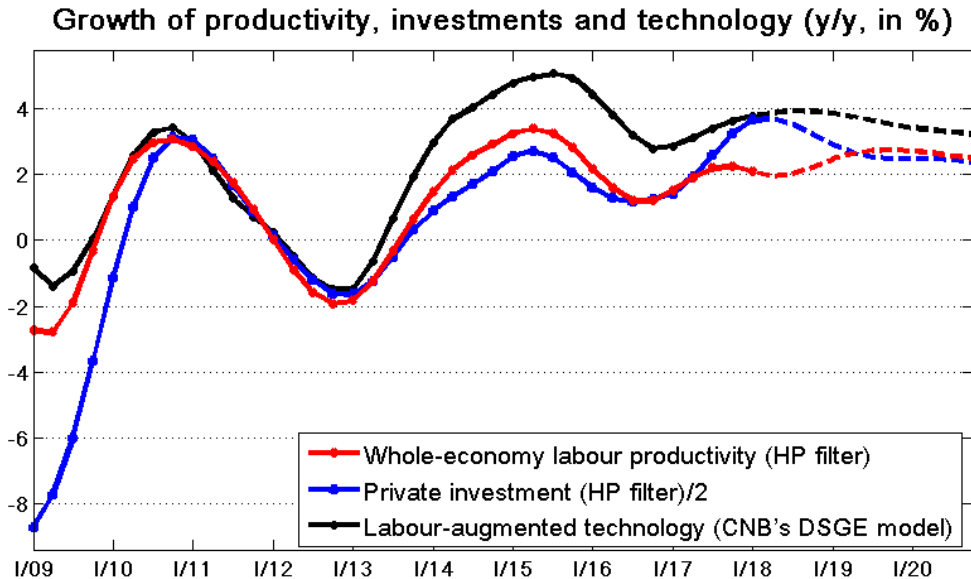


## Decomposition of labour force growth

(annual percentage change, contribution in pp, age 15 or more)

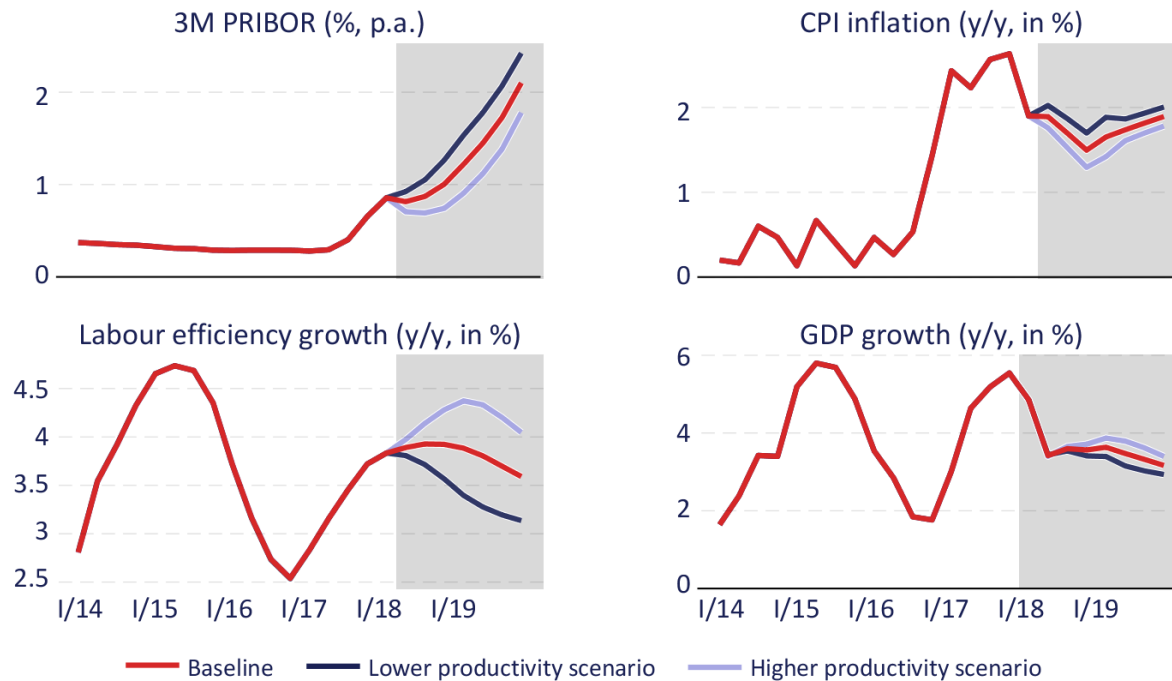


- Ongoing robust economic growth is pushing up employment, which is deepening labour market tightness. Vacancies are filled partly by the unemployed and partly by inactive persons.
- Labour force growth is driven by the participation rate, mainly due to part-time employment (group of elderly people and women with children).
- The potential labour force reserve, consisting of persons who are not actively seeking a job but are willing to work, has fallen markedly.



- The CNB assumes that the increase in (DSGE-model-filtered) labour efficiency will peak in 2018 and then gradually slow down. This is in line with private investment growth, which culminated in the first half of 2018.
- In second half of 2018, whole-economy labour productivity (HP-filtered GDP/employment) dynamics will slow slightly and will begin to converge to the pace of private investment growth at the beginning of next year.





- This scenario, in which the forecasted wage dynamics are accompanied by lower/higher labour efficiency growth, implies slightly higher/lower inflation, resulting in a higher/lower trajectory of interest rates and a consistently lower/higher GDP growth outlook.

- The Czech economy is supposed to grow faster than western countries due to the catching-up process at least in the next decade or two.
- Simultaneously, our economic situation is strongly tied to developments in our major trading partner countries.
- Therefore, risks arising from growing protectionism in global trade are highly relevant for the Czech Republic as a small open, industrial, export-oriented economy.
- So, the possible increase and spreading of protectionist measures in global trade or even trade wars between USA, the euro area and other global players represent a substantial source of external uncertainty for our economy with a potentially marked negative effect on its growth.
- But even in a small open economy, domestic economic factors and policies can sometimes cause economic activity to diverge from the balanced growth path and/or from what we observe abroad, as we have seen in our recent history.

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Petr Král

petr.kral@cnb.cz

Deputy Executive Director

Monetary Department

Czech National Bank