

BRIDGE INTERVIEW: Czech CNB head says inflation well on target

By Marek Petrus, BridgeNews

Prague--Oct. 4--The Czech National Bank is on track to meet its key net inflation target of 2.0-4.0% for 2001, assuming external inflationary pressures ease over the course of next year, central bank governor Josef Tosovsky said Wednesday. Net inflation, which excludes government-regulated prices, is the CNB's primary target for setting interest rates. The central bank's board meets Thursday to determine interest-rate policy.

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Tosovsky told BridgeNews he thought the central bank's current inflationary forecasts were realistic even in light of the recent surge in the price of oil worldwide and the strength of the U.S. dollar, both of which have fueled Czech import prices.

"I believe the current inflationary forecasts are entirely realistic, and not even the expected secondary effects of the rise in the price of imported raw materials will provide a reason for fundamental revisions," Tosovsky said in a written response to questions from BridgeNews.

In late August, the CNB raised its net inflation forecast for 2000 to 3.2-3.7% on the year from a previous estimate of 2.1-2.9%, putting it at the lower end of its end-2000 target of 3.5-5.5%.

Net inflation factors out the effects of increases in regulated prices for energy, rent and other items with controlled prices, as well as adjustments to indirect taxes and customs duties. It stood at 3.2% on the year in August.

Tosovsky said the central bank expected the net inflation indicator to come in at 2.1-3.8% next year, well within the 2.0-4.0% target for the end of 2001.

Next year, headline inflation is forecast at 4.0-5.3% on the year.

IMPACT OF HIGH OIL PRICES, STRONG DOLLAR TO EASE NEXT YEAR

Tosovsky said the predictions assumed the inflationary pressure from rising import prices would ease next year and that domestic factors such as rising demand in the recovering economy would again acquire greater significance.

"We expect the structure of inflationary pressures to change next year. The pressures related to imports will ease. Even though the relatively high crude oil prices are likely to last for some time, the fact that oil prices will not rise further will in itself favorably influence domestic inflation," he said.

"Even the continuing volatility of the koruna's exchange rate against the dollar does not have to have a significant impact on domestic inflation given the fact the koruna's exchange rate against the euro is, after all, more significant. From this viewpoint, the koruna has been stable in the long-term."

EXTERNAL IMBALANCE NOT A MAJOR WORRY FOR CENTRAL BANK

High oil prices and a strong dollar have hit the Czech economy in the past months and led to a widening trade deficit, since the Czech Republic's oil imports are denominated in the U.S. currency.

Tosovsky said, however, the CNB was not worried about the impact of external imbalances on the domestic currency given the heavy inflow of foreign direct investment, which has fully covered the country's current account deficit.

"Higher oil prices and a stronger domestic growth are worsening the current account deficit, but we do not expect this development to have any significant consequences for the koruna's exchange rate, especially when surpluses on the financial account of the balance of payments remain so strong."

He praised September's coordinated intervention by the world's major central banks to support the flagging euro, saying the move could lead to the long-term stabilization, or even some strengthening, of the single European currency.

CZECH ECONOMY TO GROW, UNEMPLOYMENT TO FALL, BUT OIL PRICE REMAINS A THREAT

The governor said global economic growth, including an upswing in the European Union, would help drive the small, open Czech economy, which is highly dependent on economic developments in the EU.

He said the Czech economy found itself in a "relatively favorable" position after recovering from a two-year recession and getting rid of the imbalances that triggered a currency crisis in 1997.

"Economic stabilization, intensifying structural reforms, continuing privatization and, last but not least, the real prospect of accession to the EU have enhanced investor interest in the Czech Republic," Tosovsky said.

"Those supply-side impulses have meant the pace of economic growth is accelerating and the rise in jobless rate is slowing down."

The central bank has forecast real annual gross domestic product growth of 1.7-2.7% for this year, and said growth could accelerate to as much as 3.7% in 2001.

Tosovsky said, however, that high oil prices remained a threat to economic growth both worldwide and at home, and thus welcomed the recent actions by major industrial nations aimed at pushing oil producing countries to boost output and help bring down global oil prices.

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Czech central bank head urges fiscal reforms to boost growth

By Marek Petrus, BridgeNews

Prague--Oct. 4--The Czech National Bank (CNB) Wednesday repeated its call to the government to revamp public finances in order to lay the groundwork for fast, sustainable economic growth in the long-term. CNB Governor Josef Tosovsky said fiscal reforms were required to ensure the country's smooth accession to the European Union, expected later this decade, and subsequently to the eurozone.

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The central bank, the International Monetary Fund and analysts have repeatedly warned that the Czech Republic's growing public sector deficit was a major threat to economic stability and have demanded sweeping fiscal reforms.

"It does not seem possible to me that this (fiscal) problem will remain unresolved," Tosovsky said in a written response to questions from BridgeNews.

"It must be obvious to anyone, including the political representation, that the looming expansion of public finance deficit will cast doubt upon the sustainability of higher growth rates that we so urgently need," he said.

The 2001 state budget draft, to be discussed in Parliament soon, projects the overall public sector deficit at 7.7% of gross domestic product (GDP) in 2000, excluding privatization revenues.

The deficit was equivalent to about 1.6% of GDP in 1999.

The Czech Republic, one of the front-runners striving to join the EU, must slash its fiscal deficit to 3% of GDP to fulfill the criteria for joining the single European currency, the euro.

In 2001, the deficit is seen easing to 6.8% of GDP.

Tosovsky said he was worried that the minority Social Democratic (CSSD) government, which faces a Parliament dominated by center-right opposition parties, would "improvise" instead of pushing ahead with major fiscal reforms.

He warned that "ad hoc" cuts in select budgetary expenditures aimed at helping to improve fiscal stability in the short-term might limit the growth potential of the Czech economy in the long-term.

"I consider also the approaching election date to be a certain problem, which always makes it hard to start pursuing more fundamental public finance reforms," he said.

The next general elections are scheduled for 2002.

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