

CNB's New Forecast

January 2007

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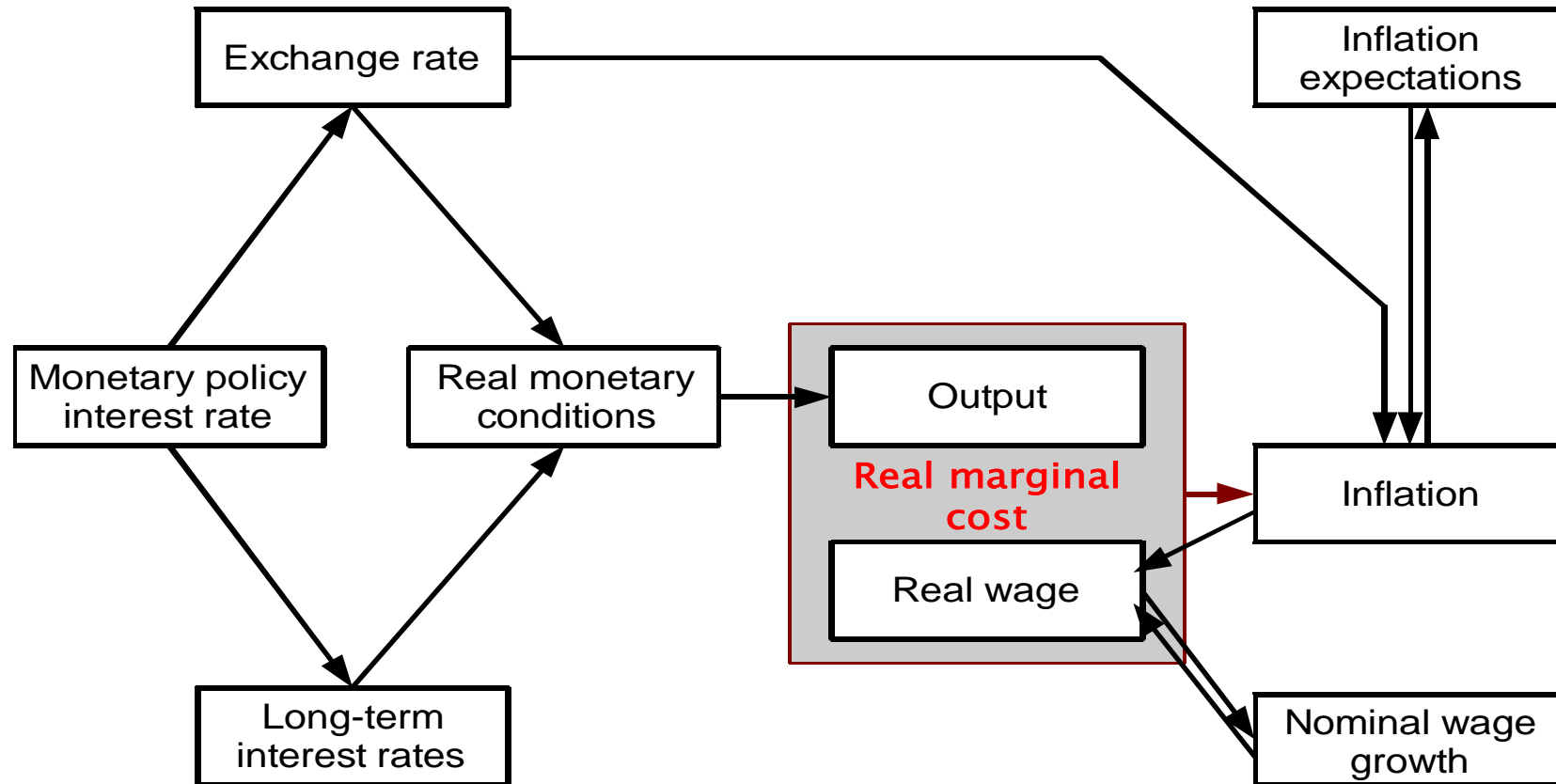
(Tomas.Holub@cnb.cz)

Meeting with analysts, Prague, 2 February 2007

Outline

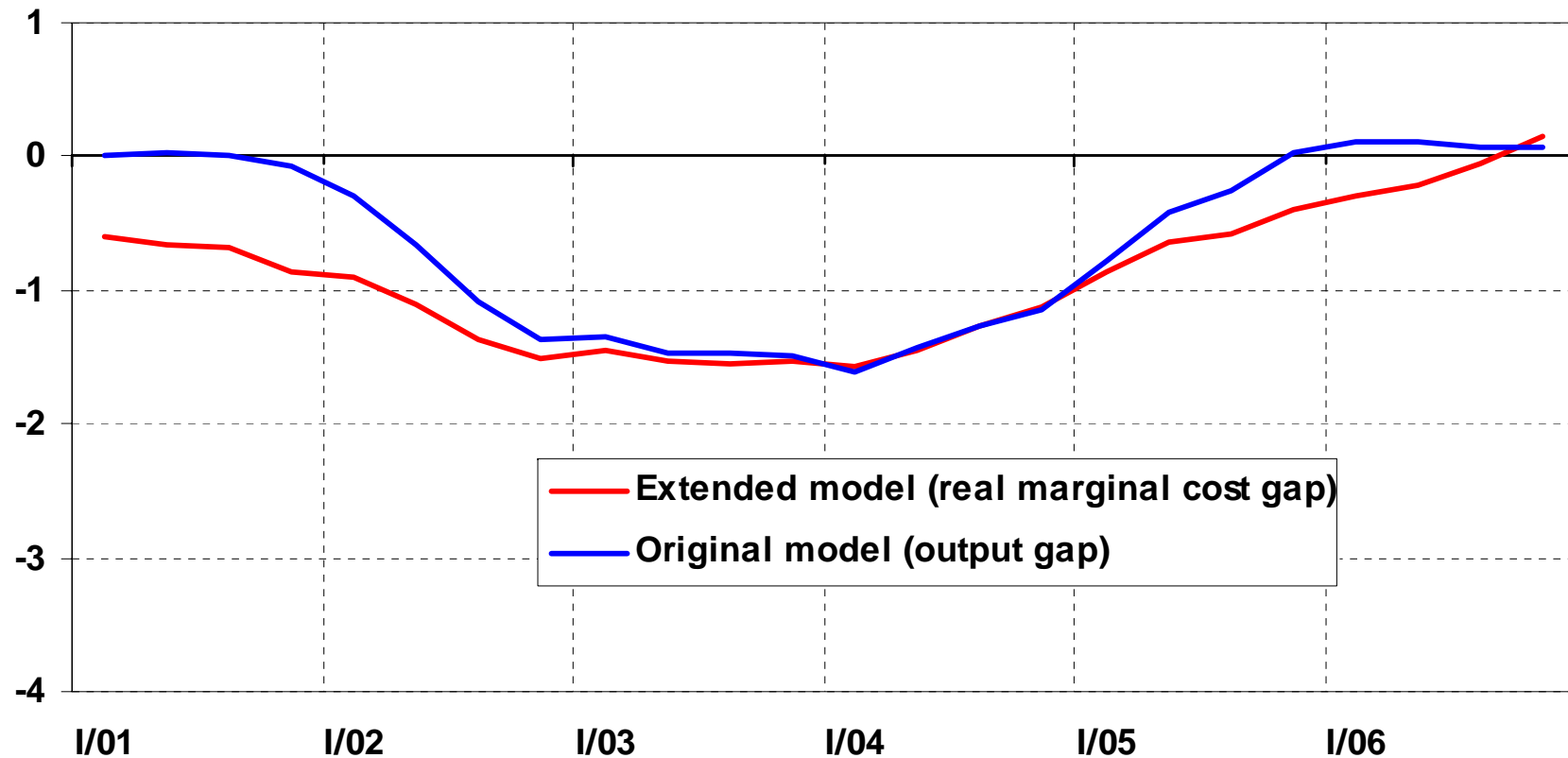
- Extended Quarterly Projection Model;
- External assumptions;
- Recent trends in inflation;
- Economic growth and labour market;
- Fiscal policy;
- Regulated prices and energy prices;
- Exchange rate and imported inflation;
- Forecast of real economy and inflation.

Extended Quarterly Projection Model



- More detailed description of inflationary pressures from the real economy, but little quantitative effect on forecast.

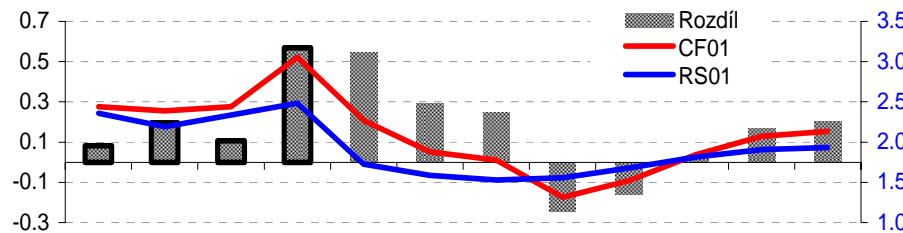
Pressures from the Real Economy



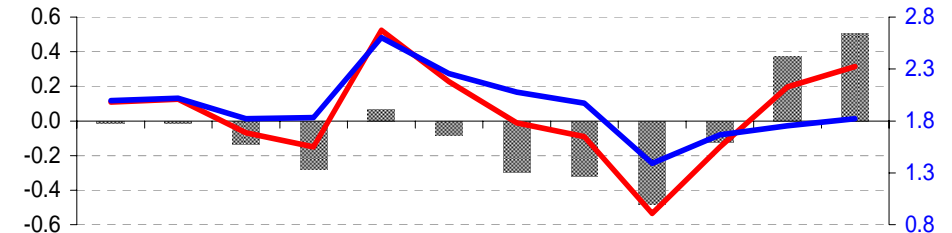
- The picture is broadly similar; Note: output gap in current model is a narrower concept than in the past.

External Assumptions (CF12)

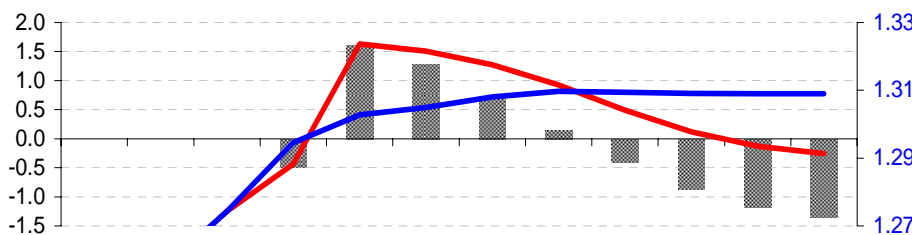
(difference in p.p.) **Eurozone effective GDP** (y/y %)



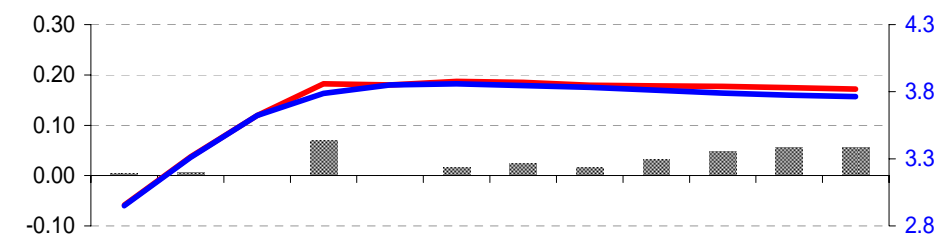
(difference in p.p.) **Eurozone effective CPI** (y/y %)



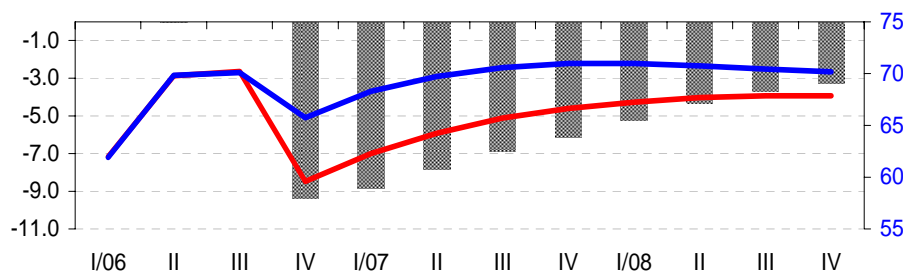
(difference in %) **Exchange rate USD/EUR** (USD/EUR)



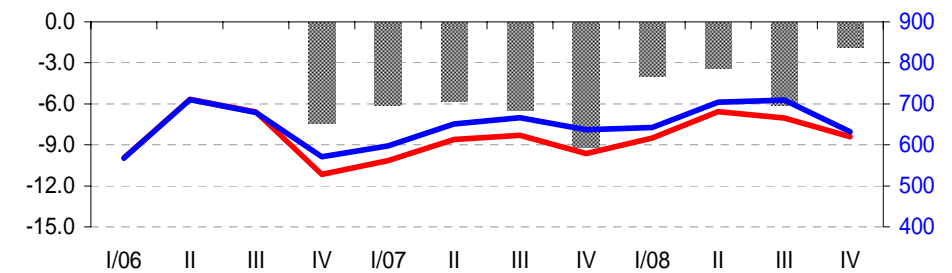
(difference in p.p.) **1Y Euribor** (% p.a.)



(difference in %) **Price of oil Brent** (USD/barrels)

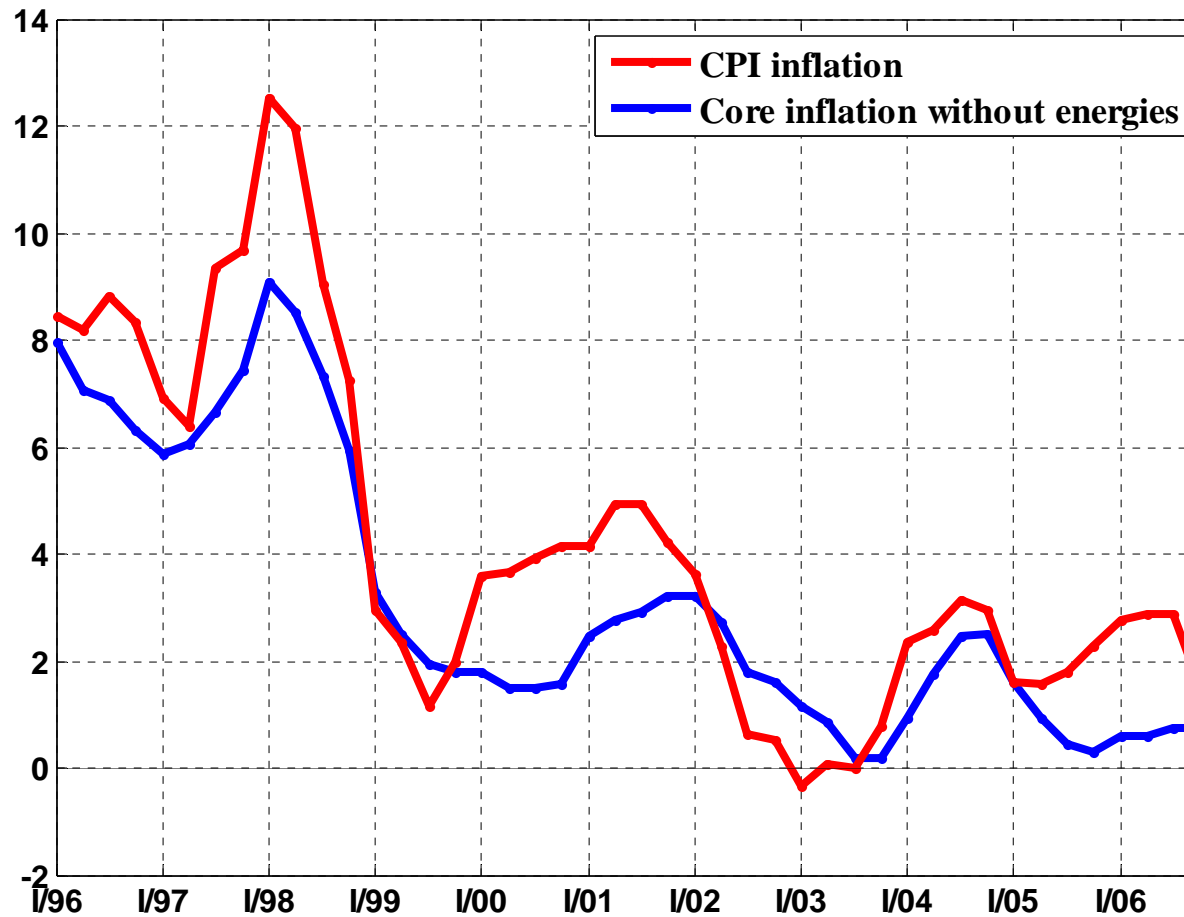


(difference in %) **Price of petrol** (USD/1000kg)



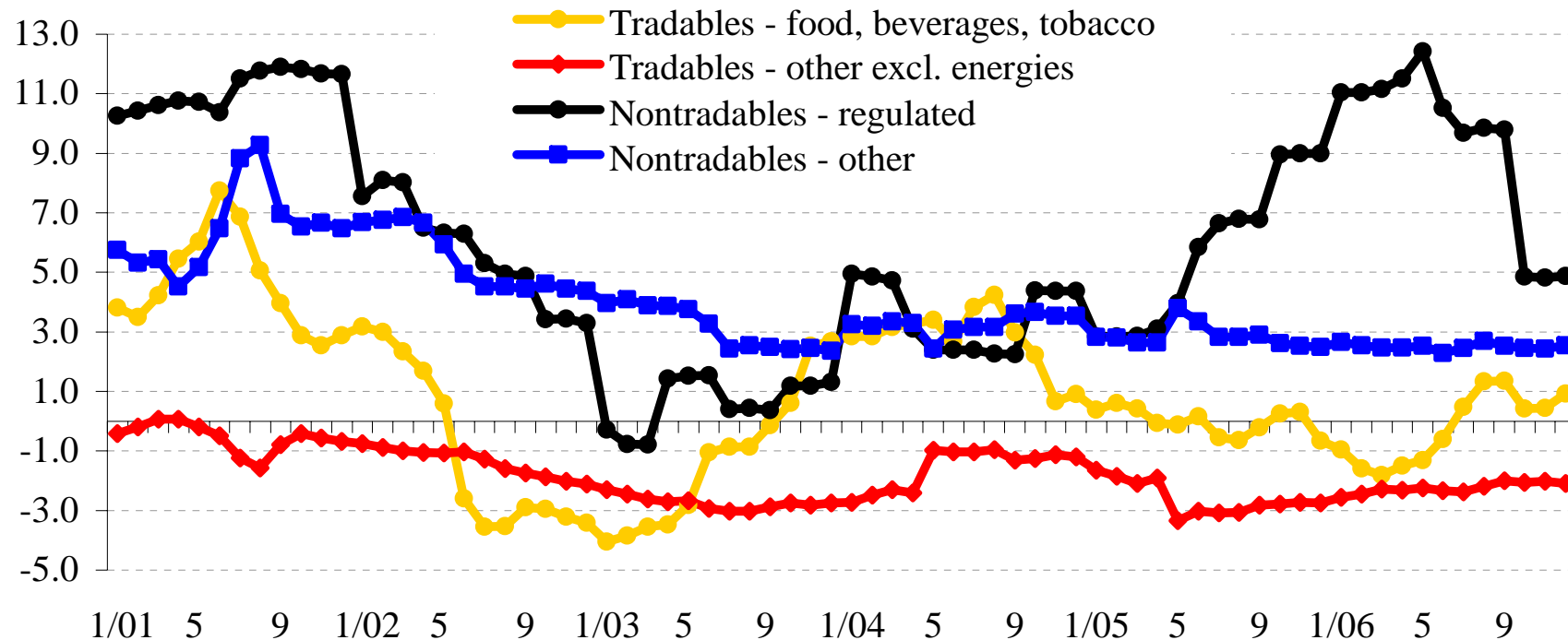
- Little impact on the forecast change (higher GDP vs. lower oil prices); CF01 also implies relatively minor changes.

Inflation



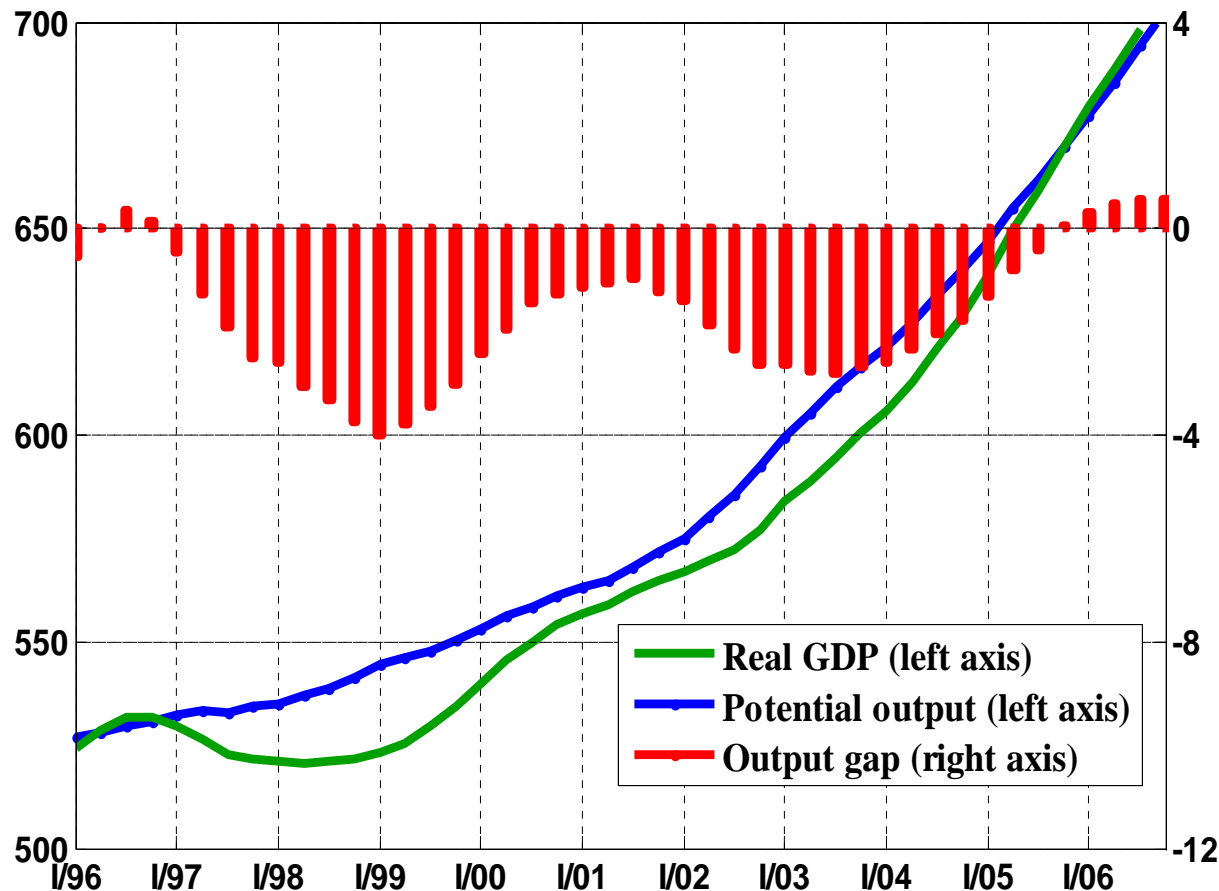
- Inflation in Q4/06 below the October forecast;
- Drop in headline inflation partly anticipated;
- Downward surprises in food prices, fuels and taxes;
- Core inflation also kept down, mainly by CZK.

Structure of Inflation (without taxes)



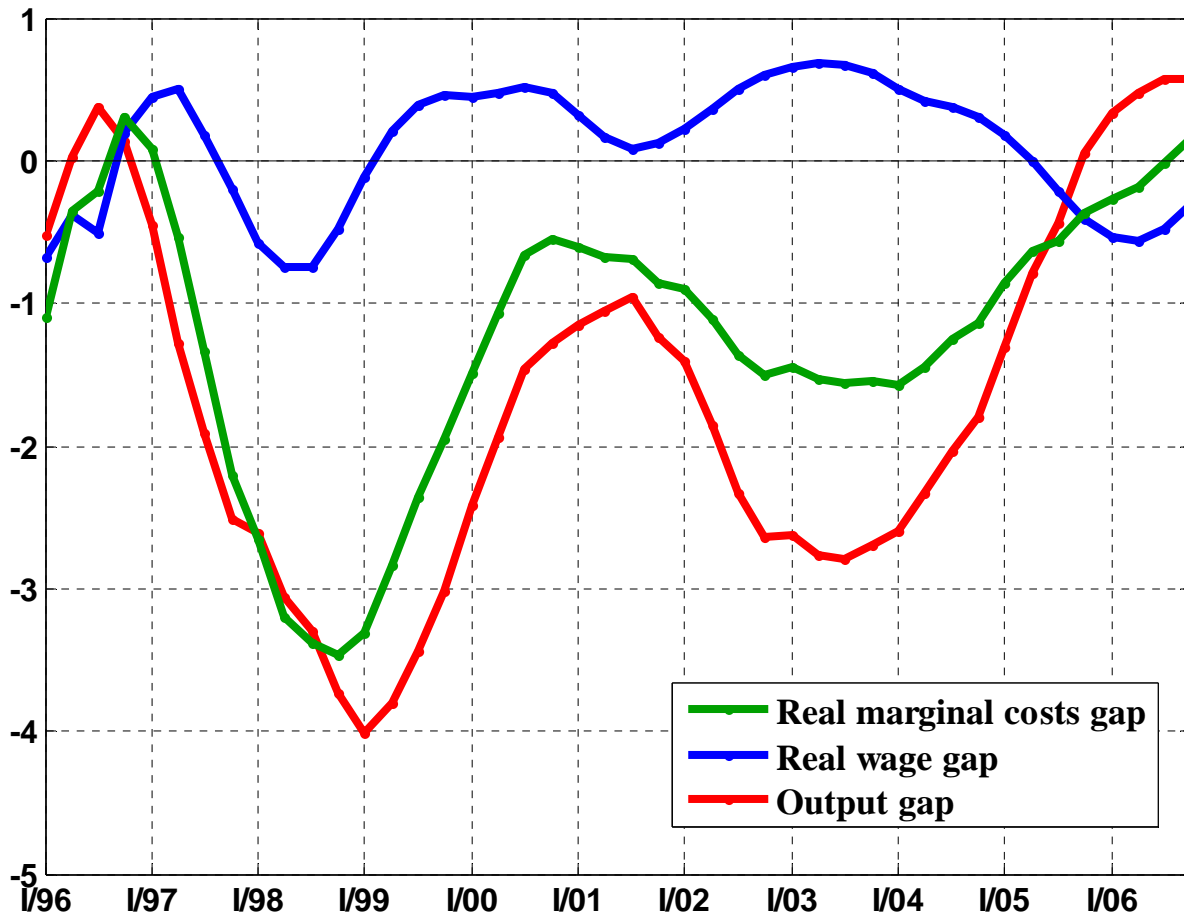
- Fast growth of regulated prices „faded away“ in October 2006;
- Food price growth volatile, difficult to predict;
- Tradables and non-tradables: quite stable developments.

GDP – Actual and Potential



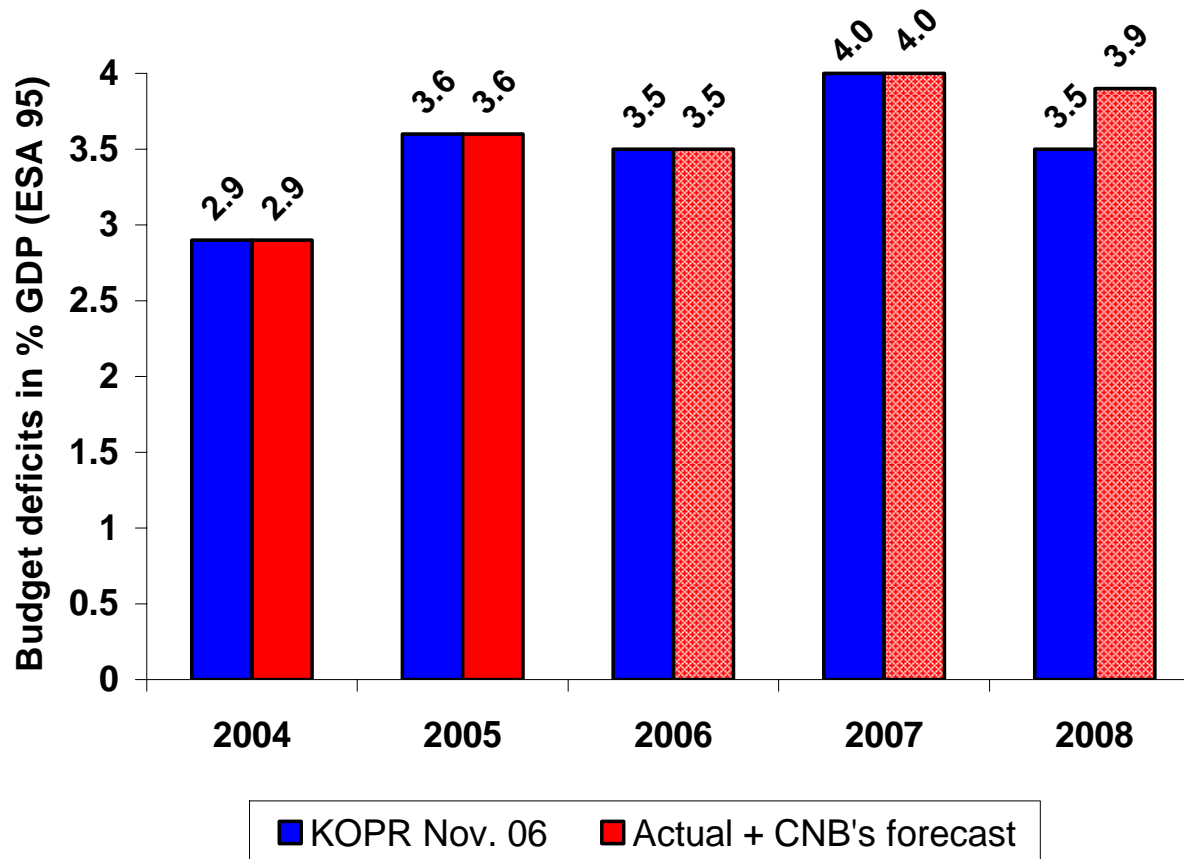
- The economy slightly above its non-inflationary potential since the turn of 2006;
- Growth currently driven by domestic demand;
- Monetary conditions broadly neutral in both components.

Pressures from the Real Economy



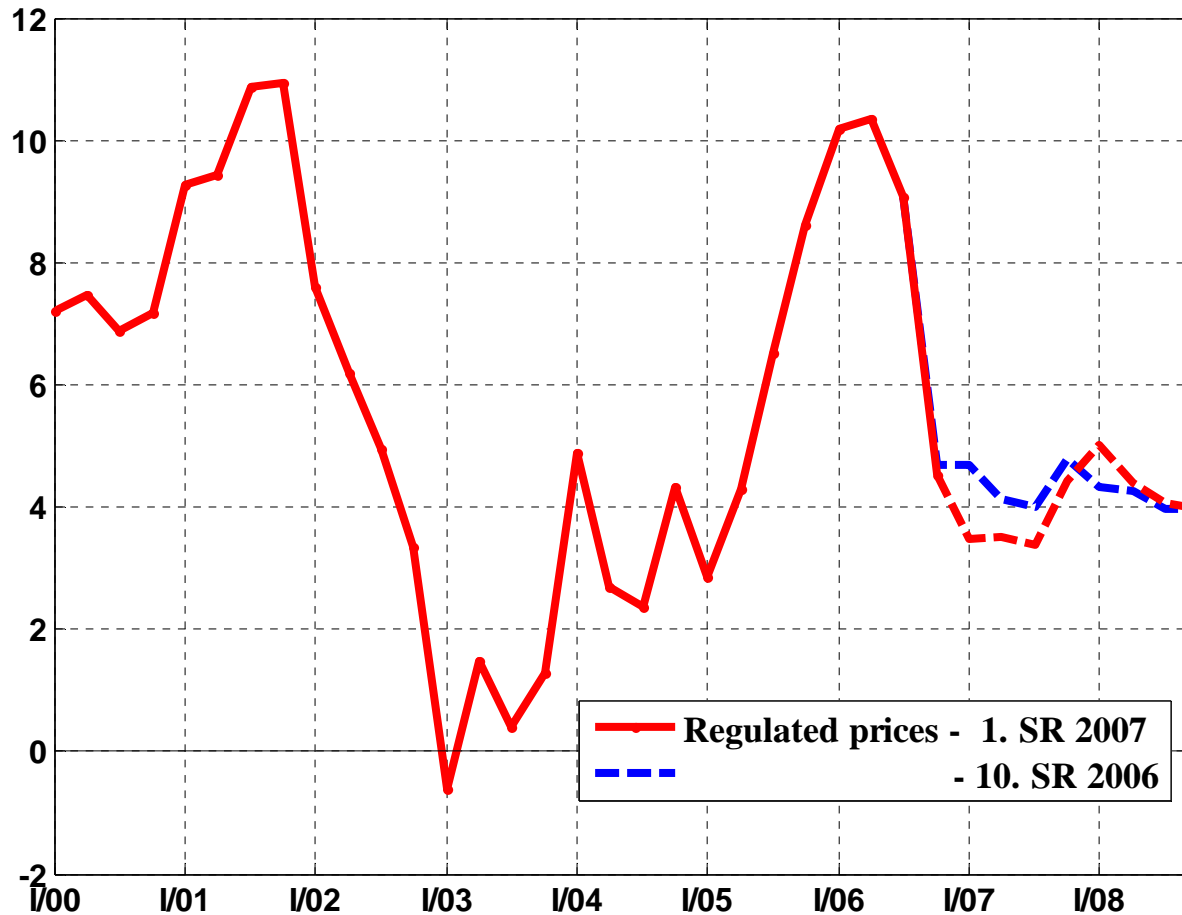
- Impact of real wages slightly anti-inflationary;
- Nominal wage growth did not accelerate in line with inflation hit by negative shocks in 2005 and 1H 2006;
- Overall pressures from real economy pro-inflationary, but only slightly.

Fiscal Situation



- Expansive fiscal policy in 2006-08;
- Fiscal impulse for 2008 revised to slightly more expansionary;
- New government program more ambitious, but uncertainty about details.

Regulated Prices

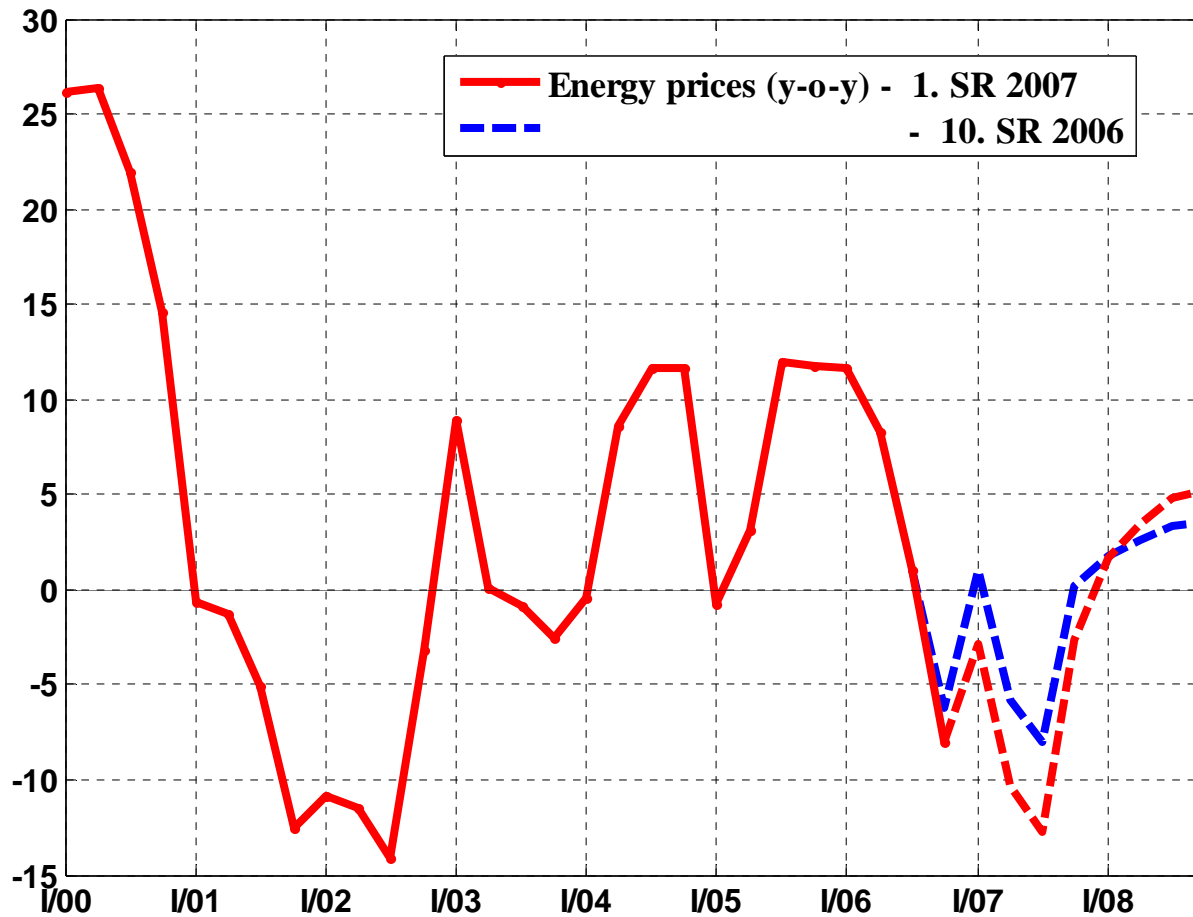


- Outlook only slightly lower for 2007 (energy prices);
- Together with taxes, contribution to inflation: 2.0 p.p. end-2007, 1.5 p.p. end-2008.

Administrative Measures (selected items and total impact)

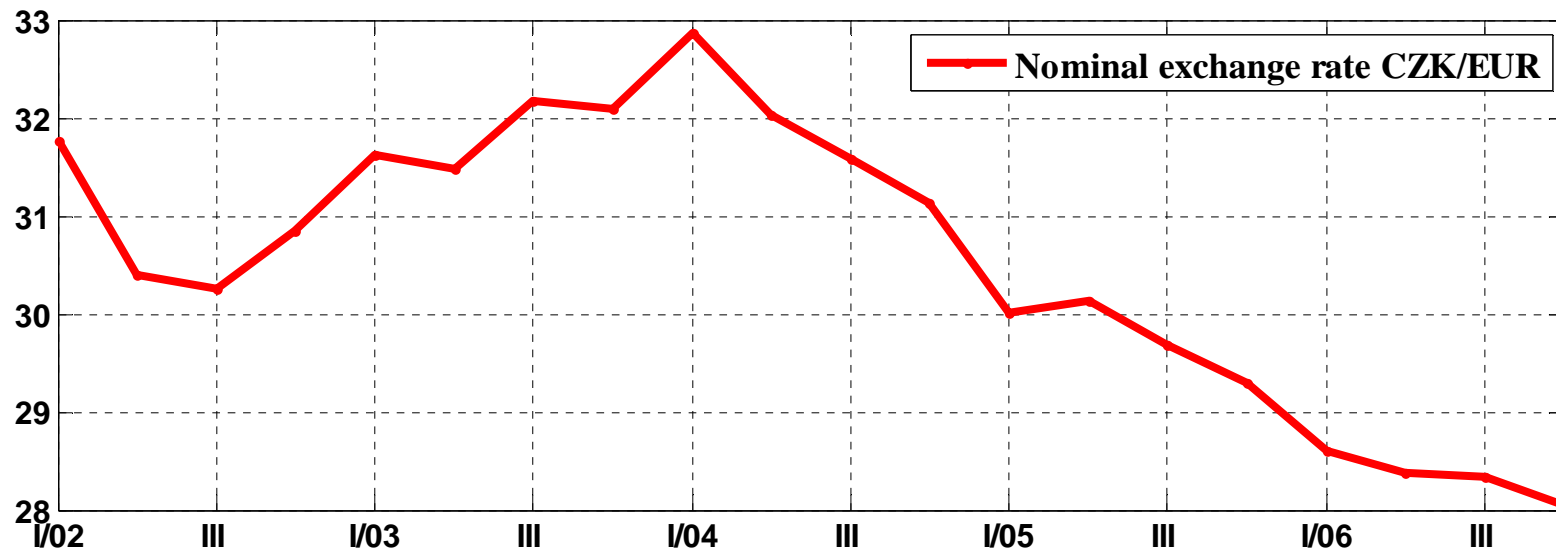
Year/date	Indirect taxes		Regulated prices		
	Item	Impact on CPI inflation	Item	Change in price	Impact on CPI Inflation
2006-Total		0,16 p.p.		4,9%	1,08 p.p.
2007	Excise duties on tobacco products	1,00 p.p.	Electricity	7,9%	0,35 p.p.
1Q 2007	(delayed impact: 1Q+2Q+3Q)		TV	20,0%	0,10 p.p.
			Regulated rents	19,2%	0,38 p.p.
			Heating	1,0%	0,04 p.p.
Total		1,00 p.p.		4,5%	1,00 p.p.
2008	Excise duties on tobacco products	0,59 p.p.	Electricity	7,0%	0,33 p.p.
1Q 2008	(delayed impact: 1Q+2Q)		TV	12,5%	0,07 p.p.
			Regulated rents	15,0%	0,35 p.p.
			Heating	1,5%	0,06 p.p.
Total		0,59 p.p.		4,1%	0,93 p.p.

Energy Prices



- Forecast lowered due to falling market gasoline and oil prices;
- Risk skewed to the downside at the moment.

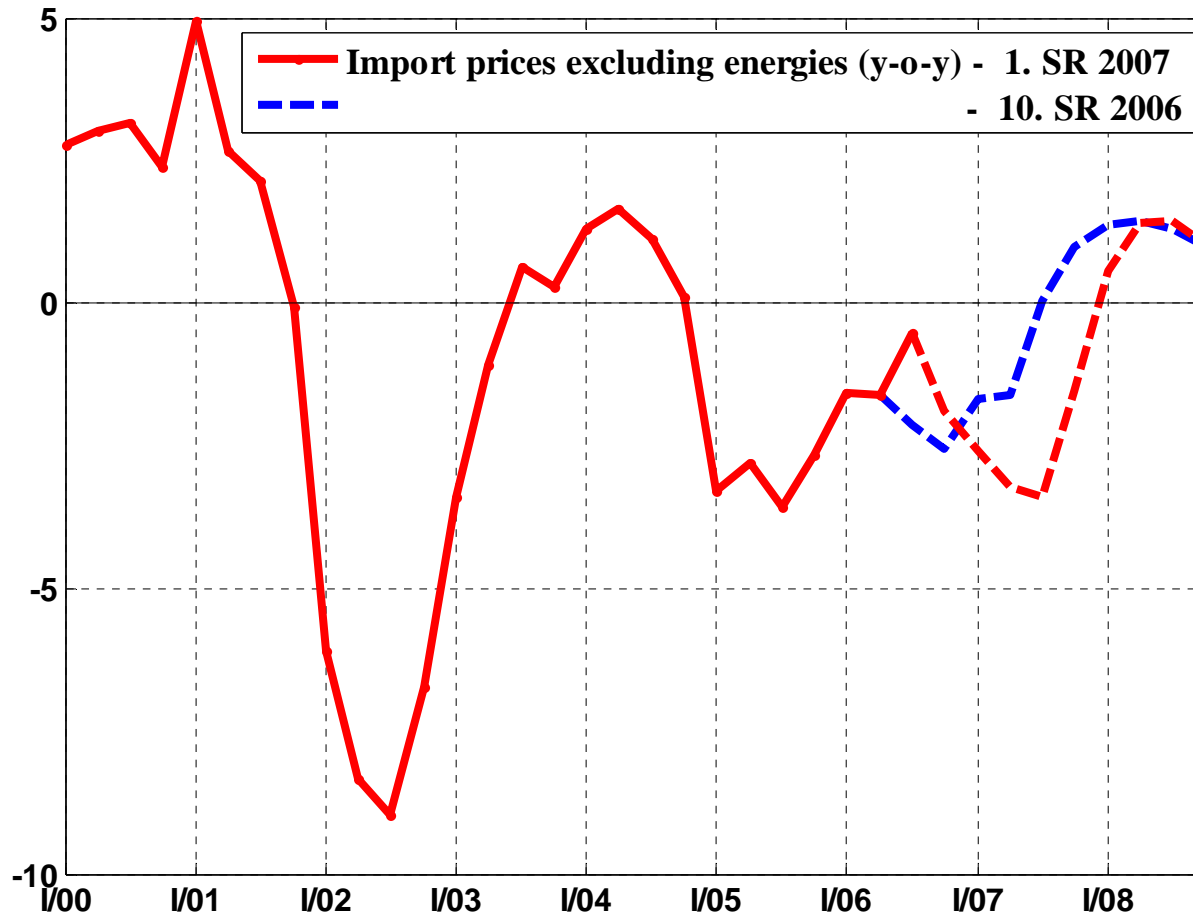
Exchange Rate



External forecasts of CZK/EUR

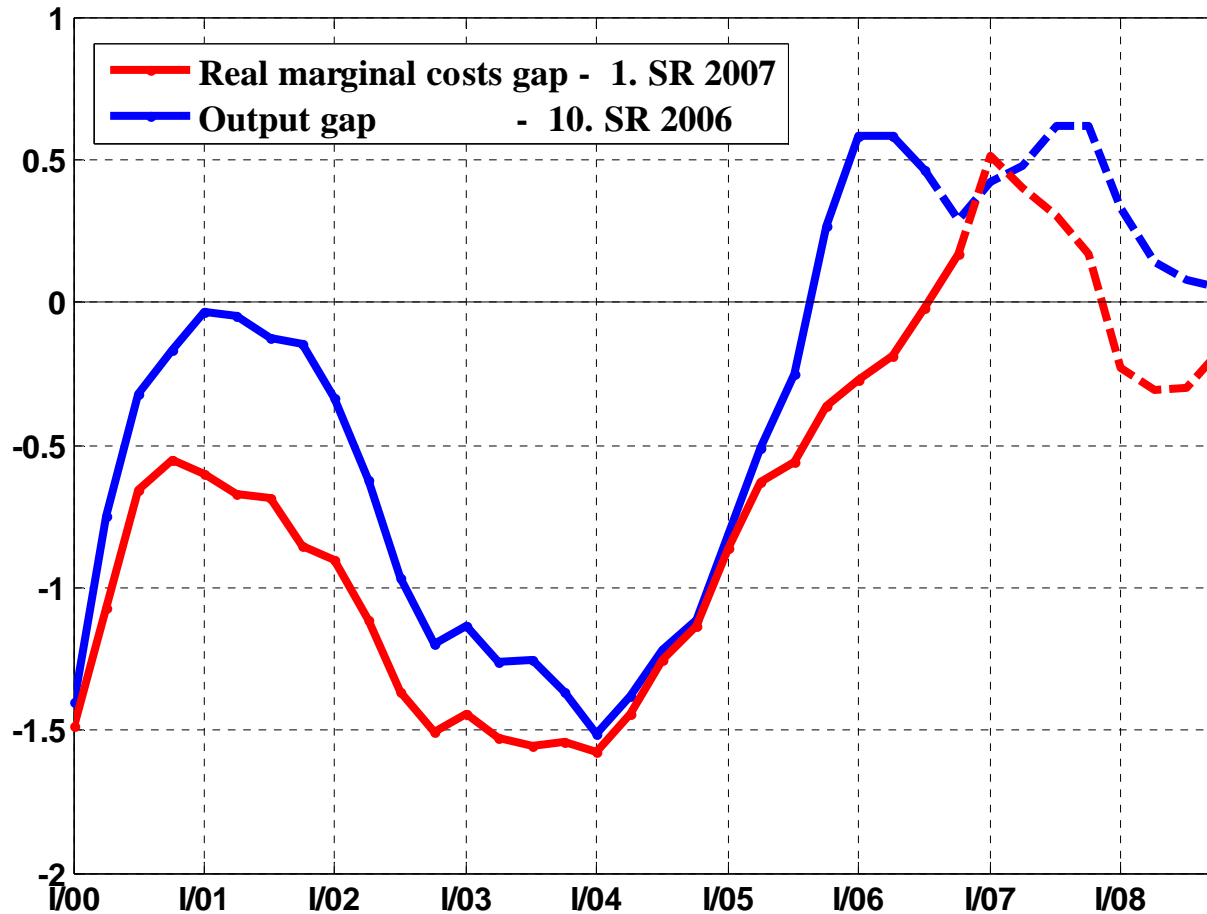
Date of forecast	Next quarter	1Y horizon	
	CF	Financial market	CF
1/06	29.1	28.3	28.8
4/06	28.7	27.9	28.2
7/06	28.5	27.7	28.0
10/06	28.2	27.6	27.8
1/07	27.5 (1Q07)	27.1	27.6

Import Prices excl. Energy



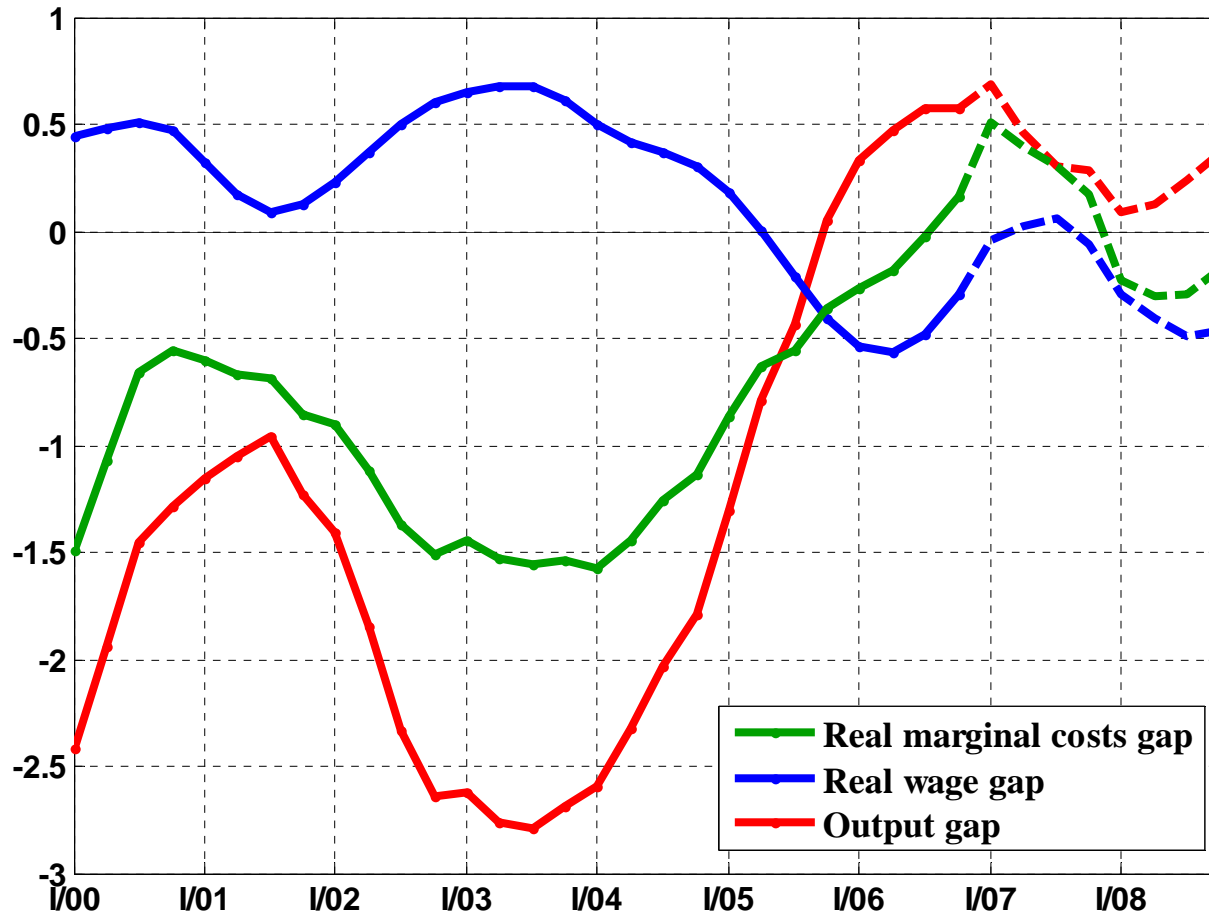
- Lower forecast reflects stronger CZK level and lower outlook for foreign inflation;
- Still expected to move from anti-inflationary to slightly pro-inflationary impact in 2008.

Pressures from the Real Economy



- Assessment of the current situation similar to October forecast;
- Lower pressures expected in the future (in 2008 even slightly anti-inflationary).

Pressures from the Real Economy



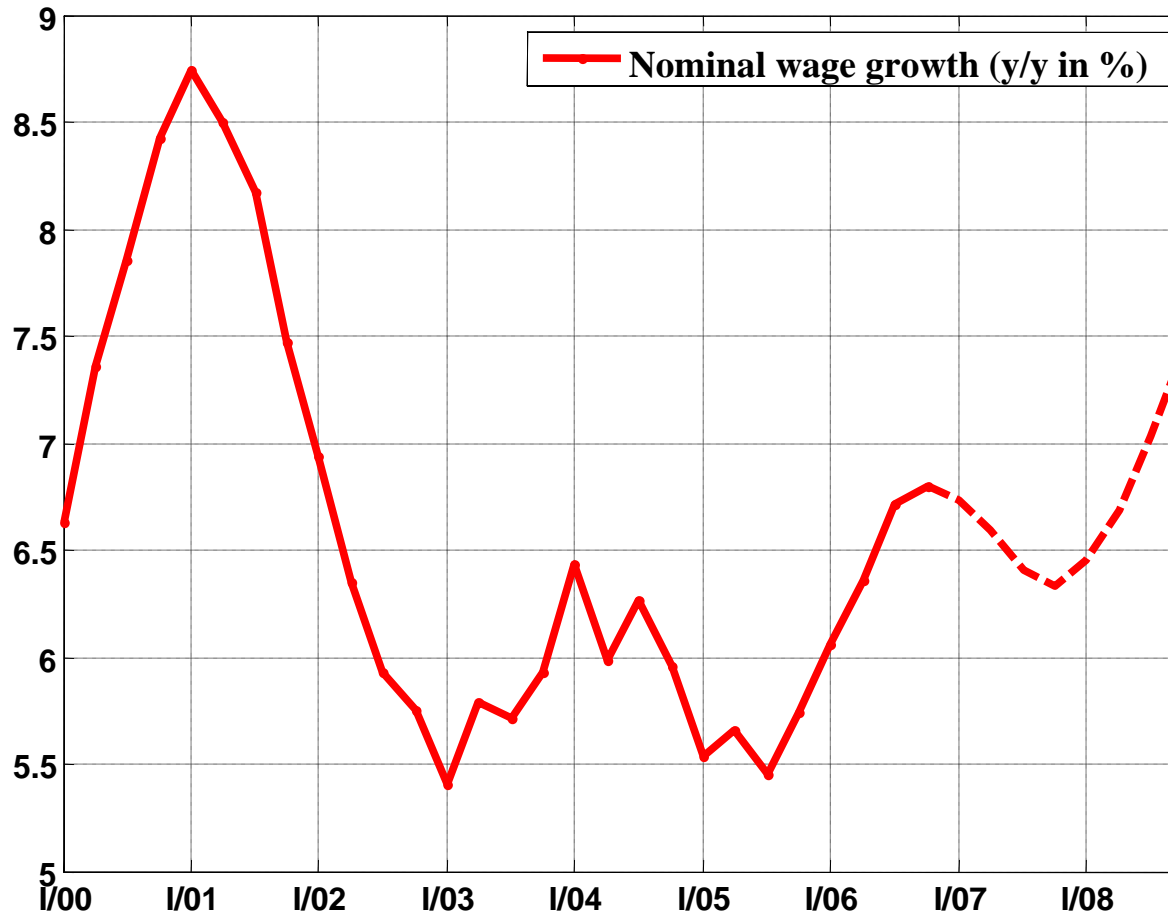
- Output gap will remain slightly positive (decline in 2007 caused mainly by weaker growth in EU);
- Real wages will move back to slightly anti-inflationary impact.

GDP Growth Forecast

y/y change	2006	2007	2008
Gross domestic product	6.0	5.3	4.8
Household consumption	4.2	4.0	3.7
Government consumption	-0.2	1.7	0.6
Fixed investment	7.3	8.7	7.9
Exports	14.2	11.0	11.2
Imports	13.3	10.6	10.7

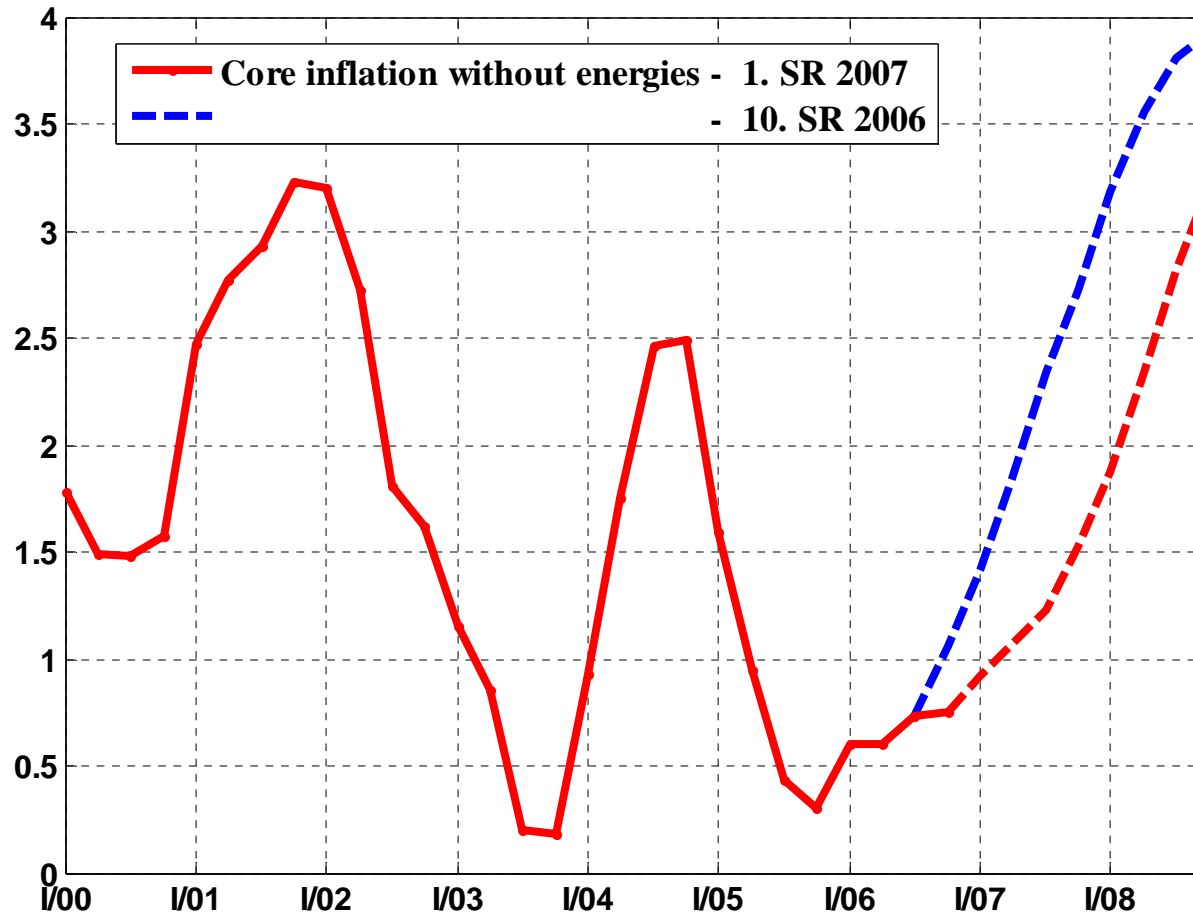
- GDP growth will slow down towards 5 % in 2007-08;
- Forecast revised slightly down for 2007-08;
- Consumption growth will remain at around 4 % in 2007;
- Fixed investments growth will remain high;
- Net exports' contribution will be modestly positive.

Nominal Wage Growth



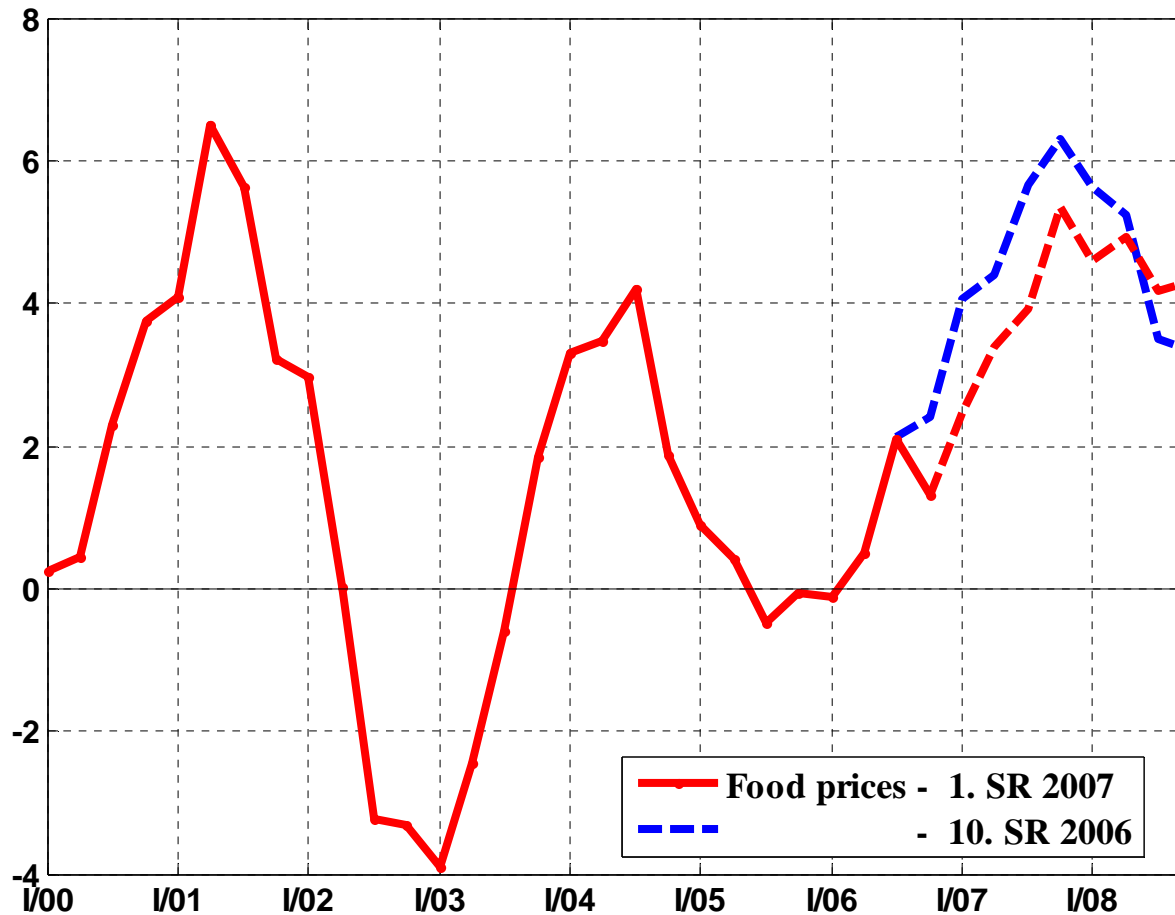
- Growth rate of average nominal wage in business sector will slightly moderate in 2007 (to 6.6 %);
- Re-acceleration expected for 2008 (to 7.1 %).

Core Inflation



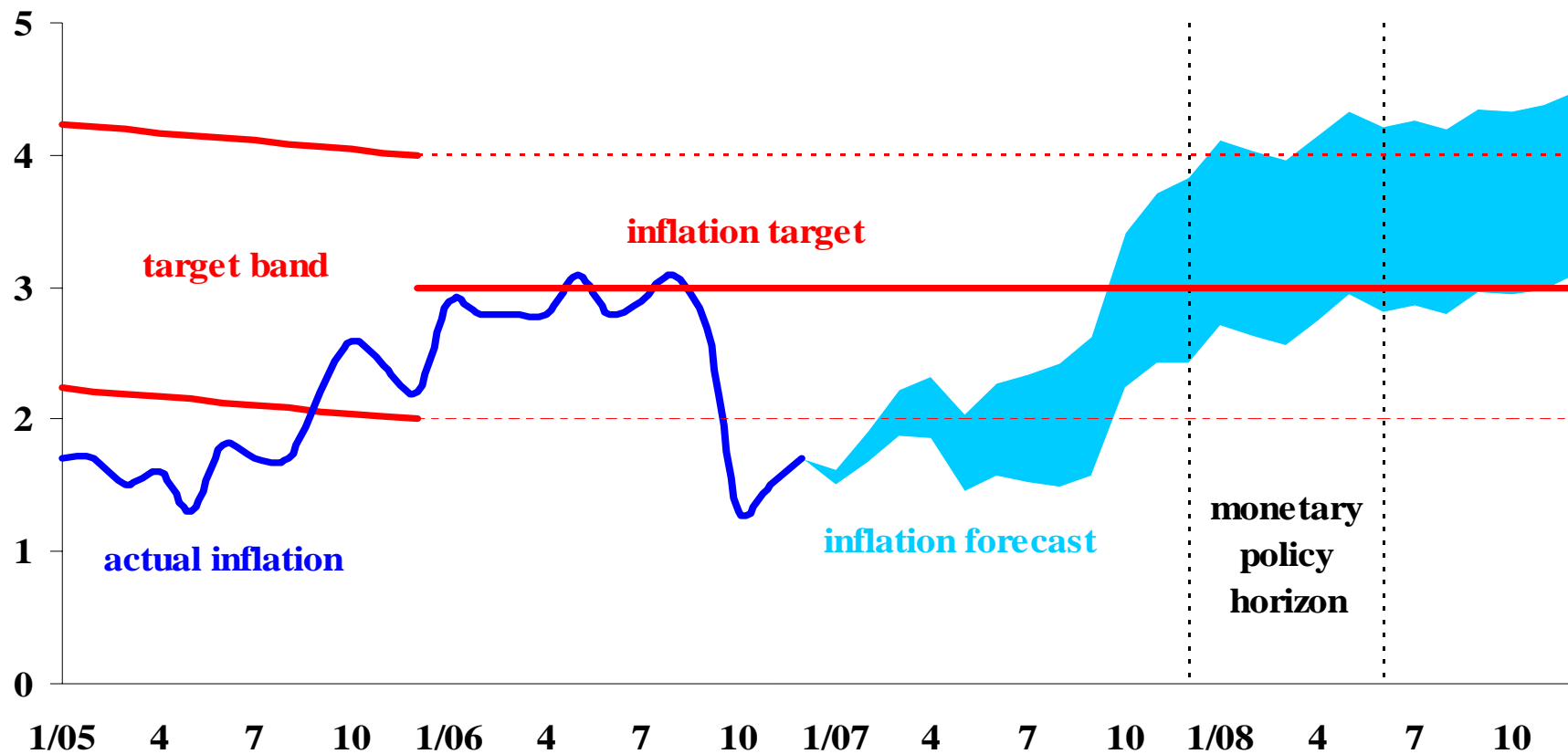
- Lower forecast reflects lower inflation in Q4/06, expected deeper decline in import prices ex energy and weaker pressures from the real economy;
- But acceleration still expected.

Food Prices (including taxes)



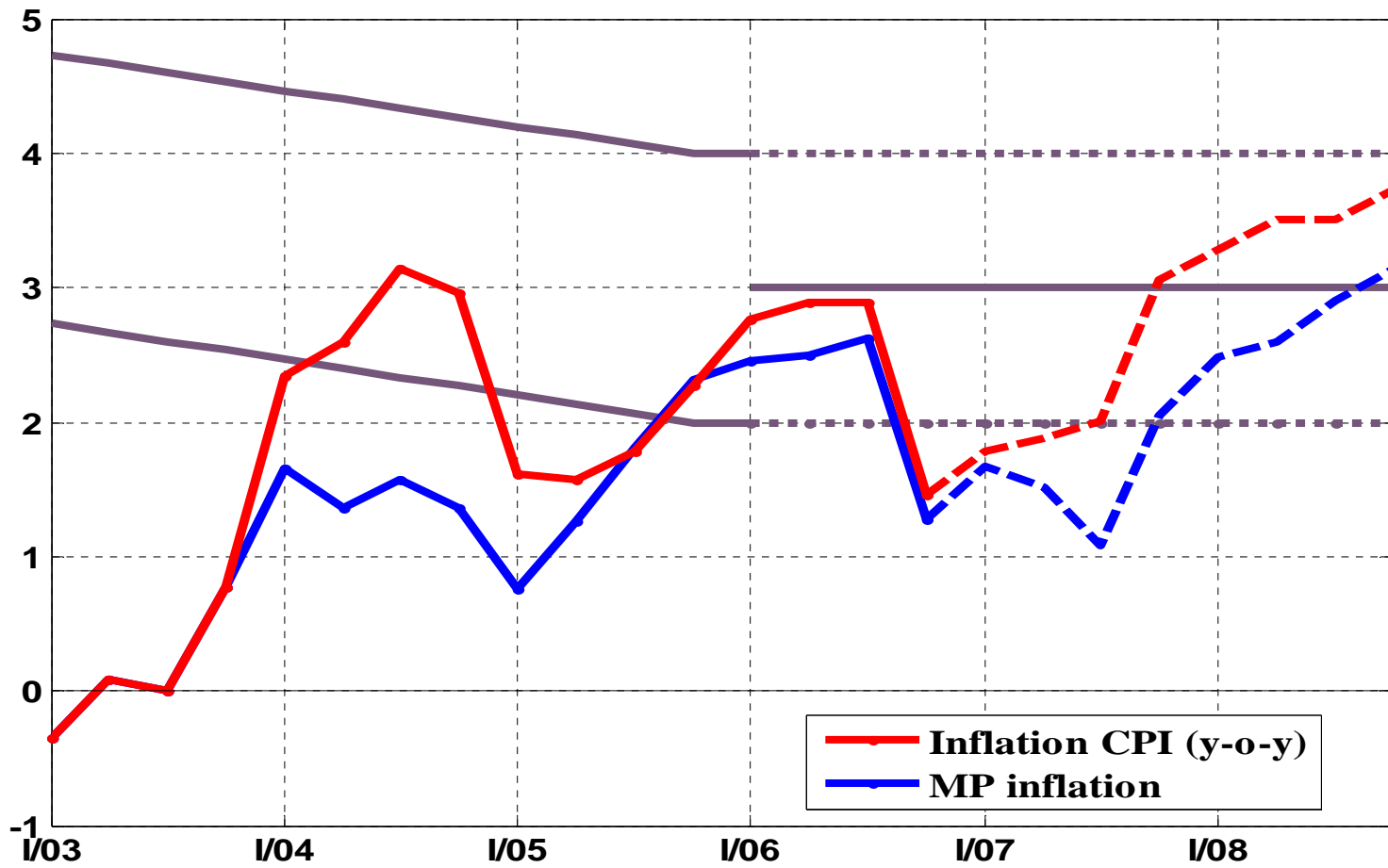
- Outlook also lowered due to similar factors as for core inflation, modified timing of tax changes and lower agricultural prices in 2006/07.

Overall Inflation



- Consistent with the forecast and its assumptions is broad interest rate stability initially and then a gradual rise in nominal interest rates at the forecast horizon.

Inflation Net of Tax Changes



Thank you
for your attention.