



CNB's New Forecast (Inflation Report I/2011)

Meeting with Analysts

Tomáš Holub

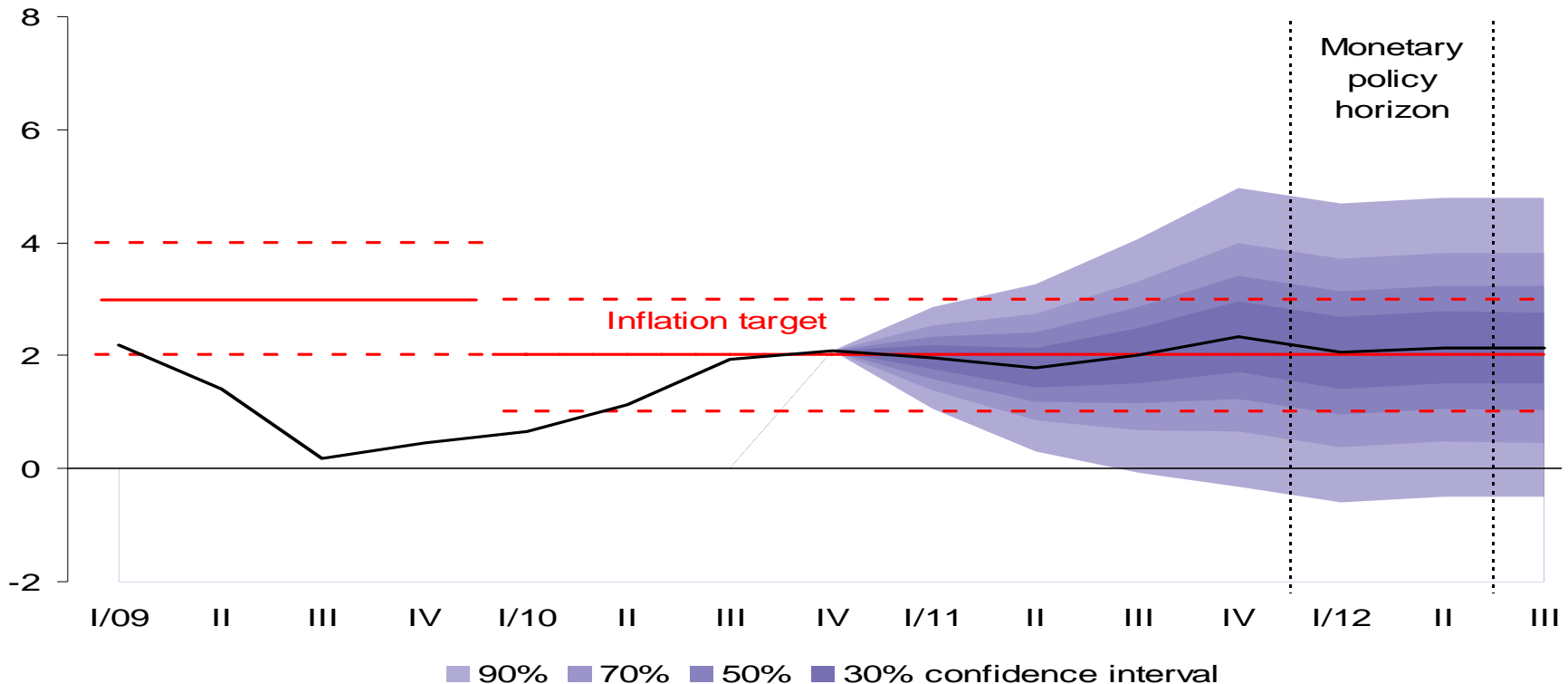
Prague, February 11, 2011

Summary of the Inflation Forecast

- Inflation will remain close to the 2% target.
- Food price growth will speed up further in the near term. Core inflation will turn positive in 3Q 2011. The growth of administered prices will remain around 4%.
- In the EA, interest rates will gradually increase, while a moderation in the currently high growth of both the GDP and PPI is expected.
- Some inflationary pressures will start to emerge gradually due to faster wage growth, economic recovery in 2012 and increasing profit margins. Import prices will reflect the gradual CZK appreciation.
- The GDP will grow by 1.6% in 2011 and 3.0% in 2012. The labour market is still relatively weak and its recovery will be uneven.

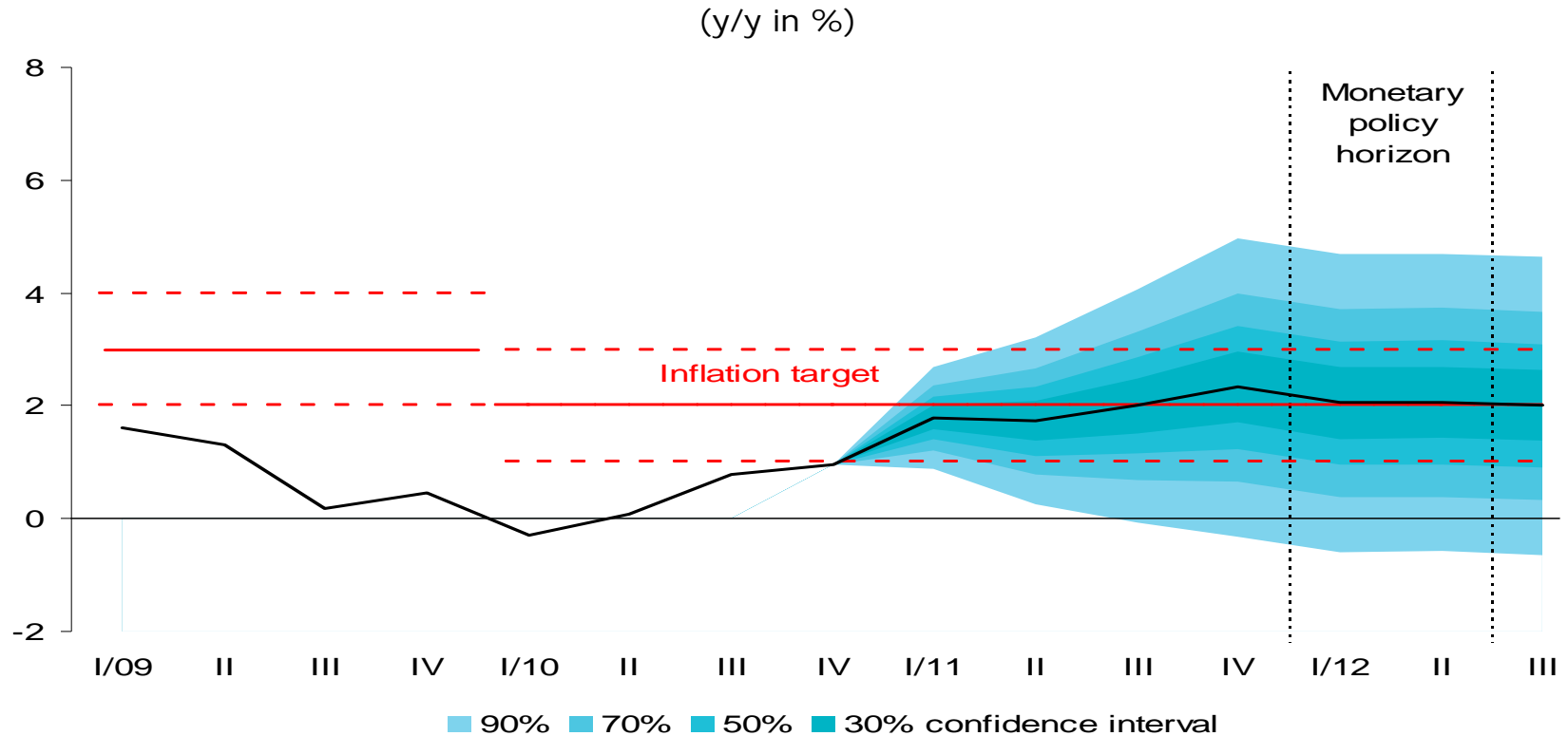
Headline Inflation Forecast

(y/y in %)



- Inflation forecast stays close to the 2% target during the entire forecast horizon.

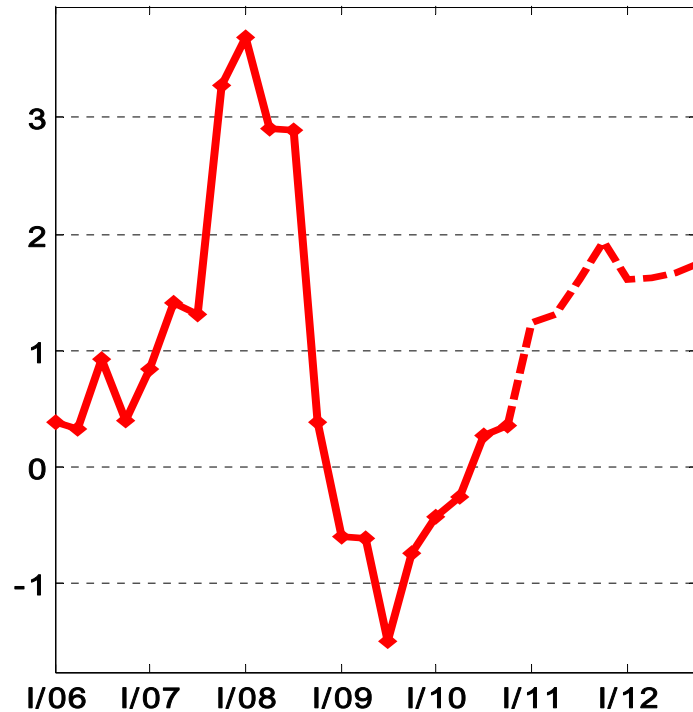
MP-Relevant Inflation Forecast



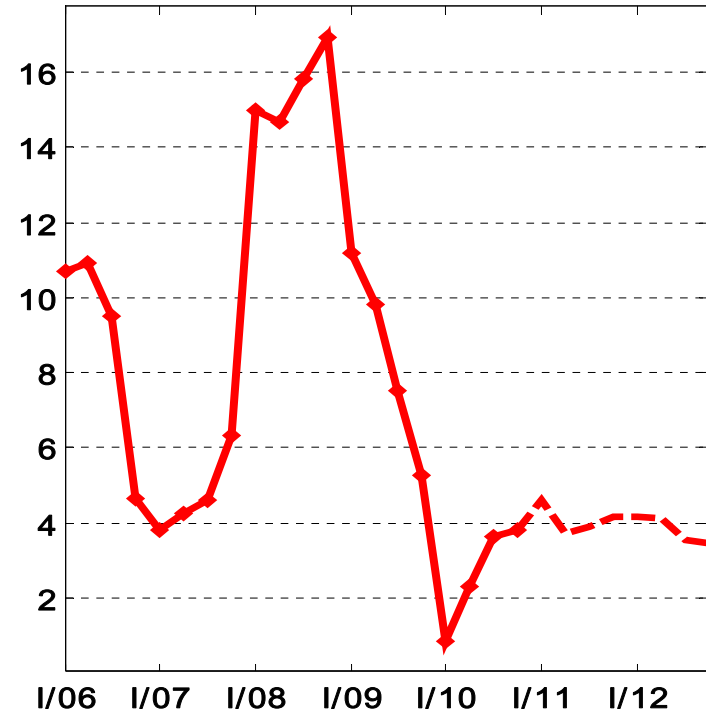
- MP-relevant inflation will increase to the target and stay there for most of the forecast horizon.

Market and Administered Prices

Net Inflation (y/y, in %)

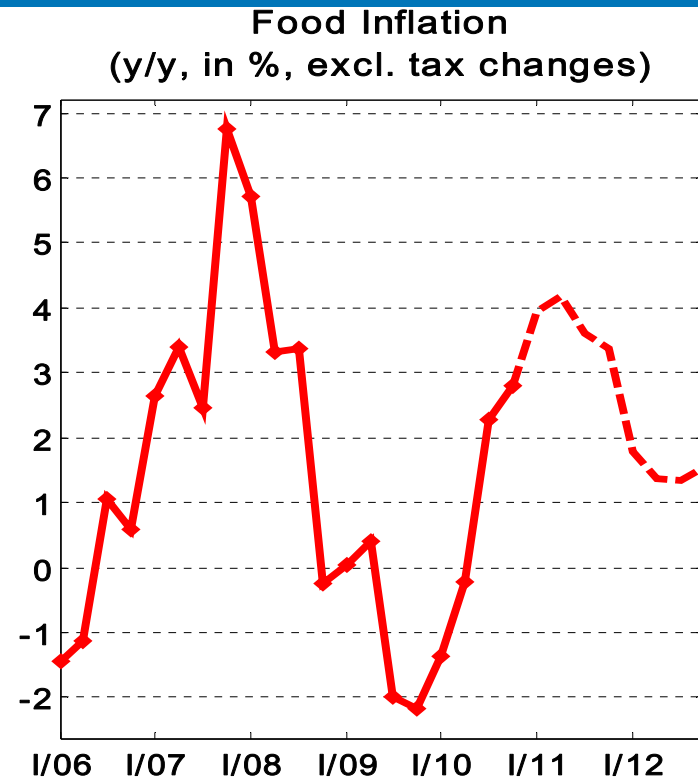
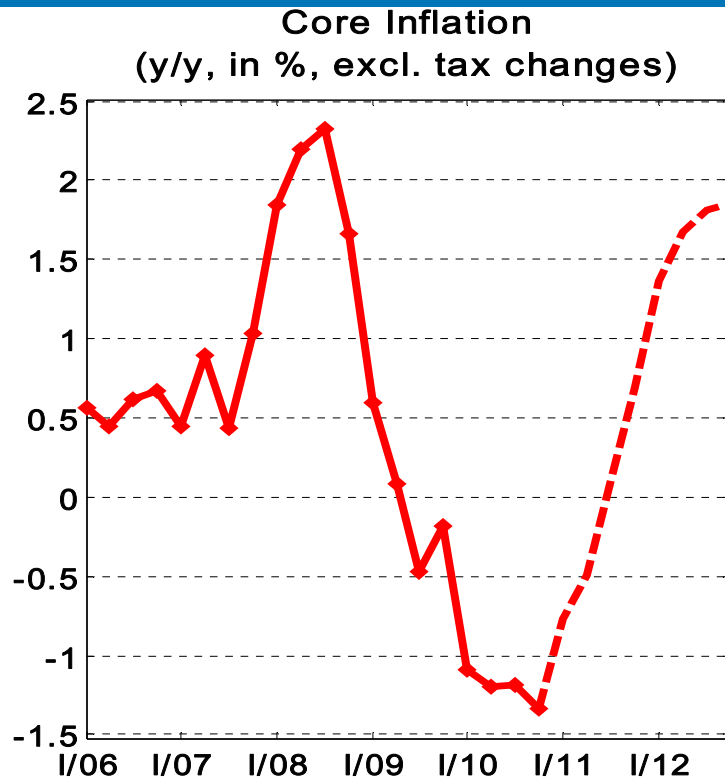


Growth of Administered Prices (y/y, in %)



- Net inflation will gradually speed up from the low levels.
- Administered price growth will move around 4%.

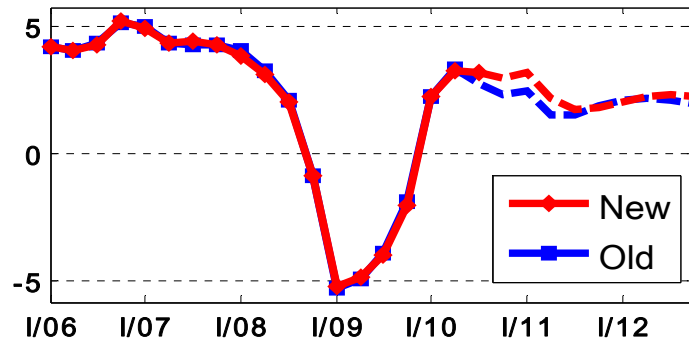
Core Inflation and Food Prices



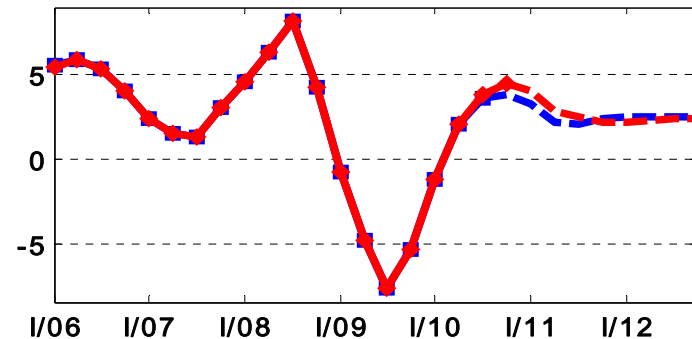
- Increasing core inflation in 2011-2012 together with the ongoing – albeit gradual – economic recovery.
- High agricultural prices \Rightarrow food prices in the near term.⁶

External Assumptions

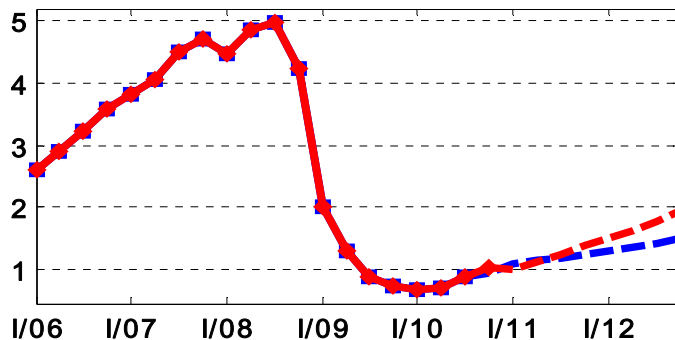
Growth Rate of GDP - Eurozone (y/y, in %)



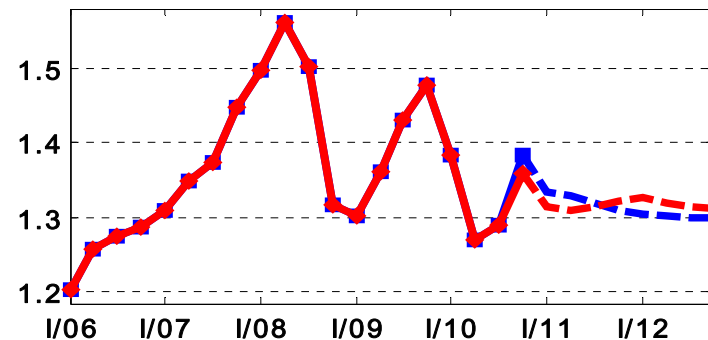
PPI Inflation - Eurozone (y/y, in %)



3M EURIBOR



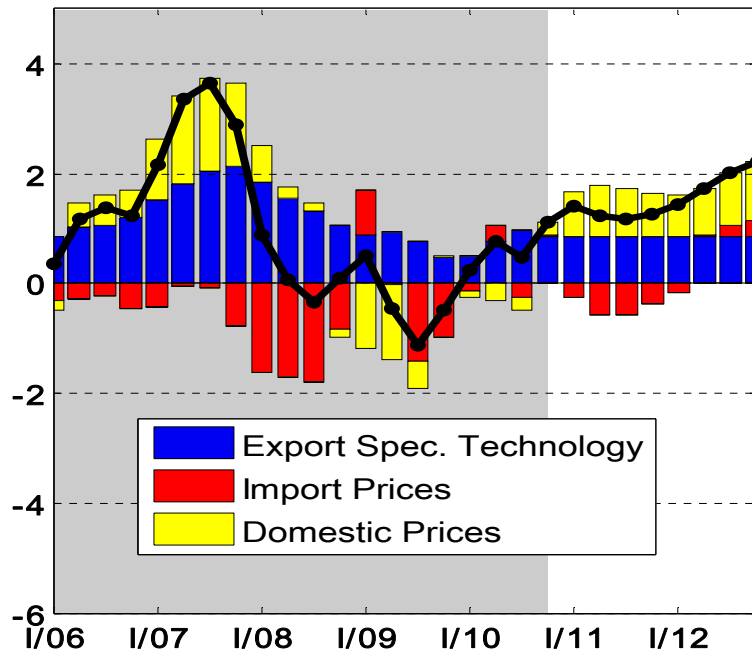
USD/EUR



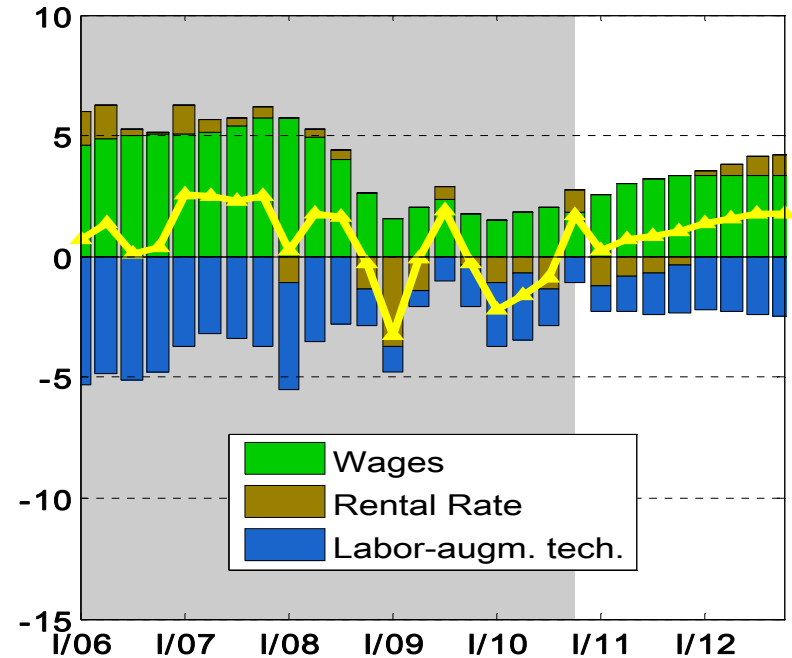
- Two key drivers of the outlook: German current solid performance and higher commodity prices.

Domestic Costs vs. Import Prices

Nominal Marginal Cost in Consumption Sector
(q/q, in %, ann.)

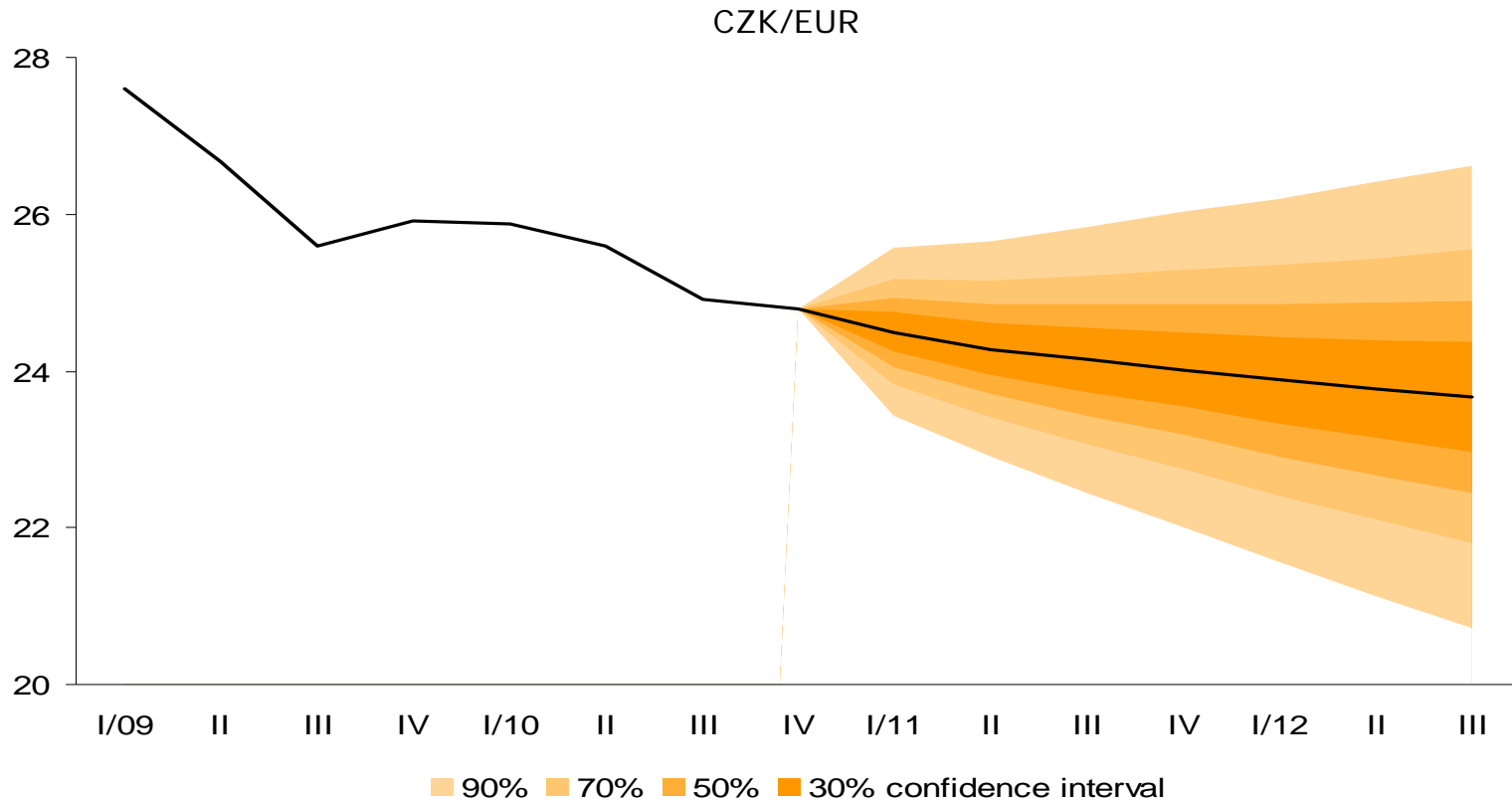


Nominal Marginal Cost in Domestic Sector
(q/q, in %, ann.)



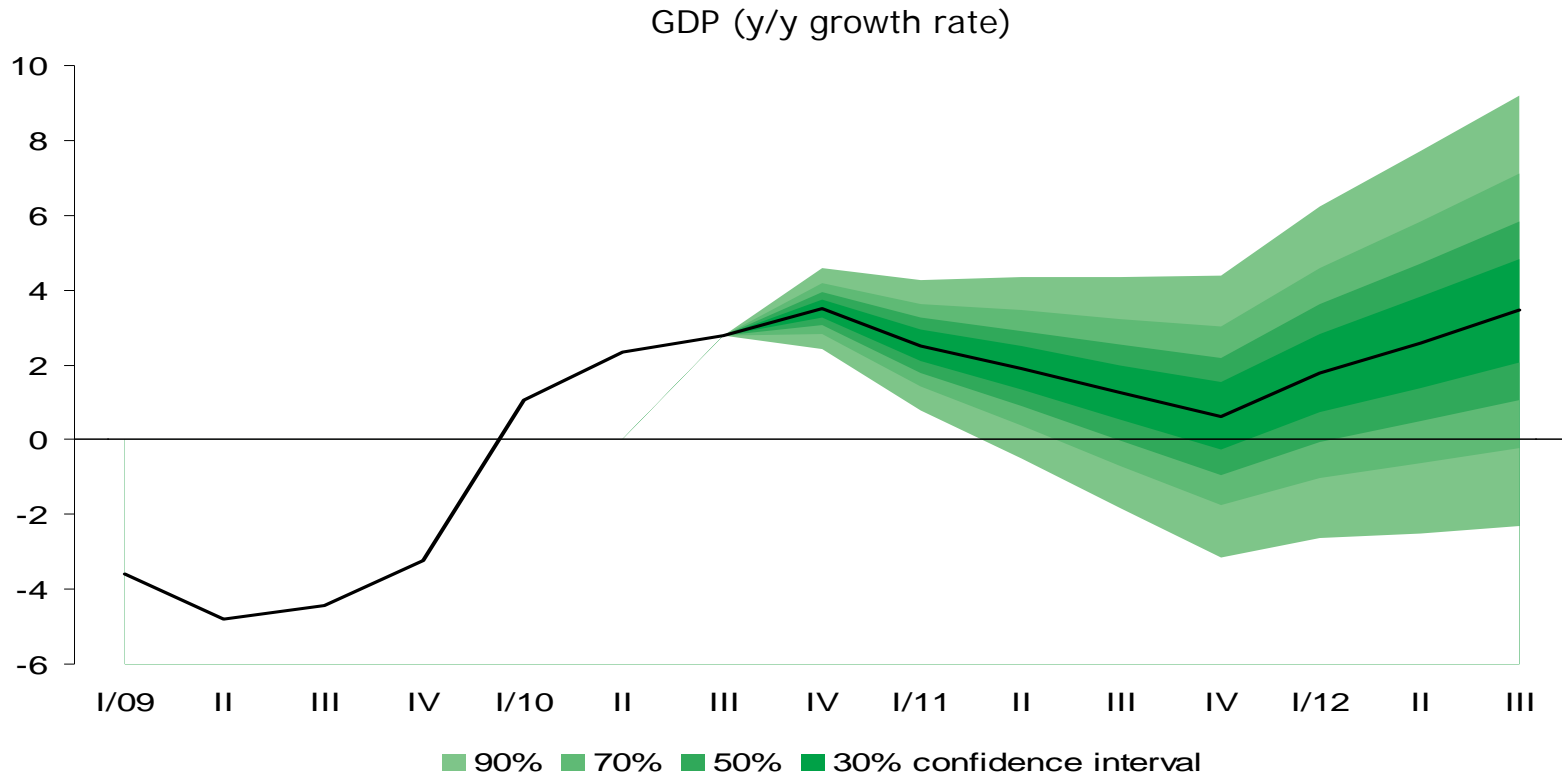
- Domestic inflation pressures currently not apparent, but will start to increase; vs. downward impact of import prices. Gradual correction of the depressed margins.

Exchange Rate Forecast



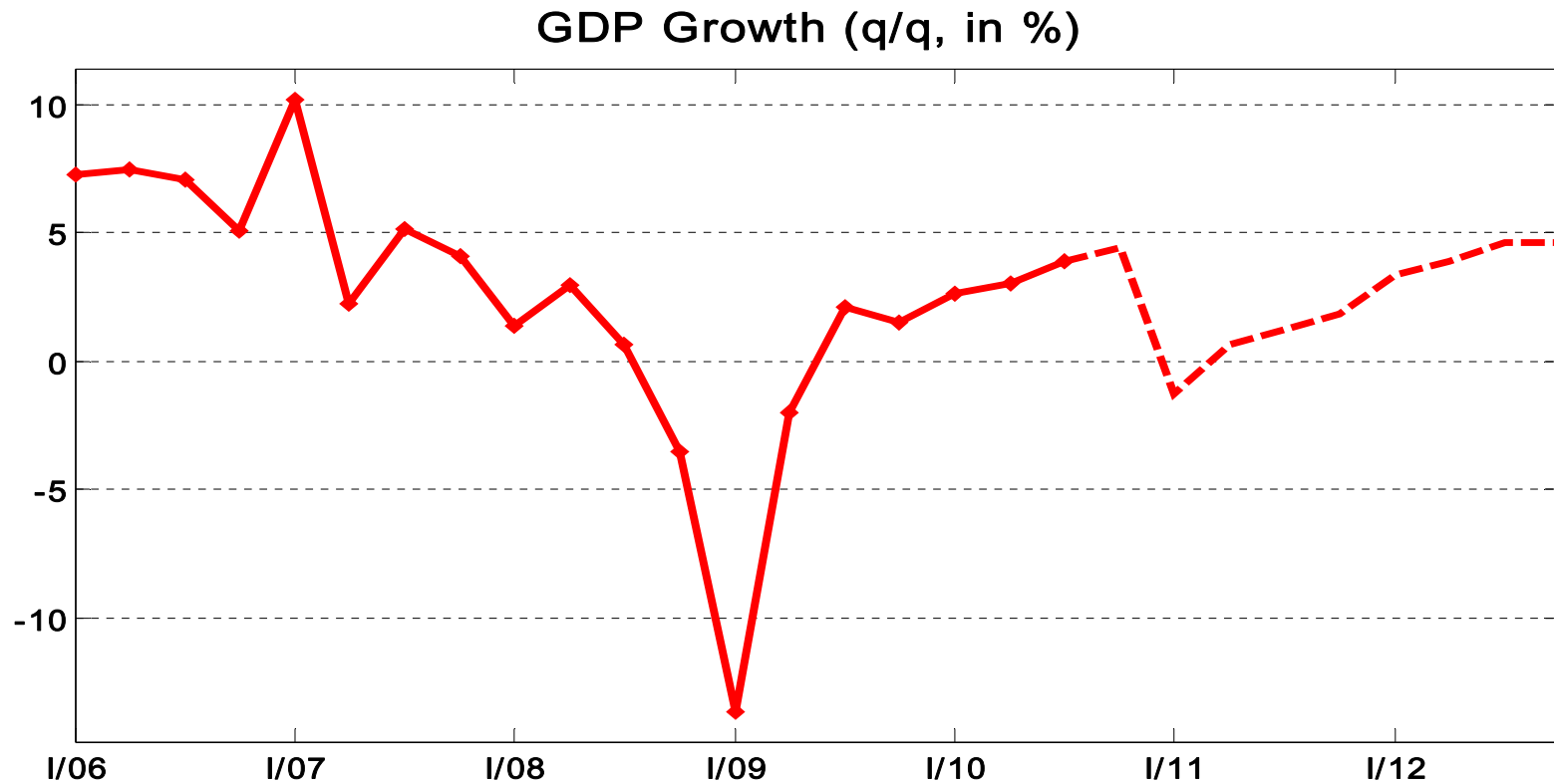
- The nominal exchange rate will gradually appreciate.

GDP Growth Forecast (i)



- The y/y GDP growth will slow down during 2011.
- Averages for 2010: 2.4 %; 2011: 1.6 %; 2012: 3.0 %.

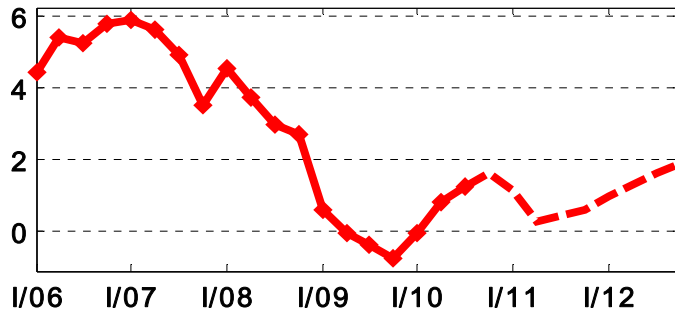
GDP Growth Forecast (ii)



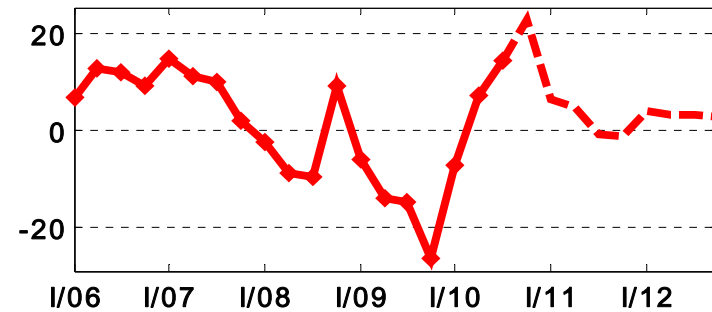
- In (annualised) q/q terms, the forecast predicts a slowdown at the beginning of 2011 due to fiscal consolidation, end of the solar boom etc.

Forecast of Aggregate Demand

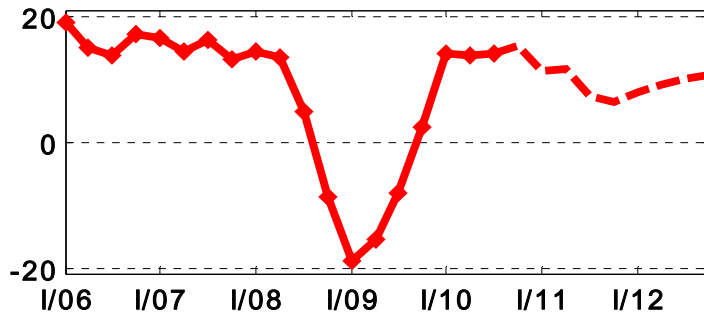
Household Consumption Growth
(y/y, in %)



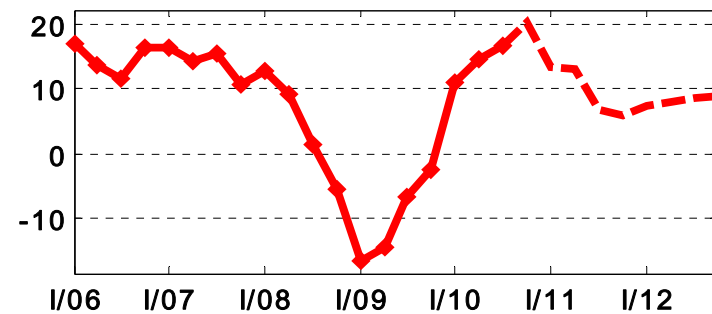
Investments Growth
(y/y, in %)



Exports Growth
(y/y, in %)

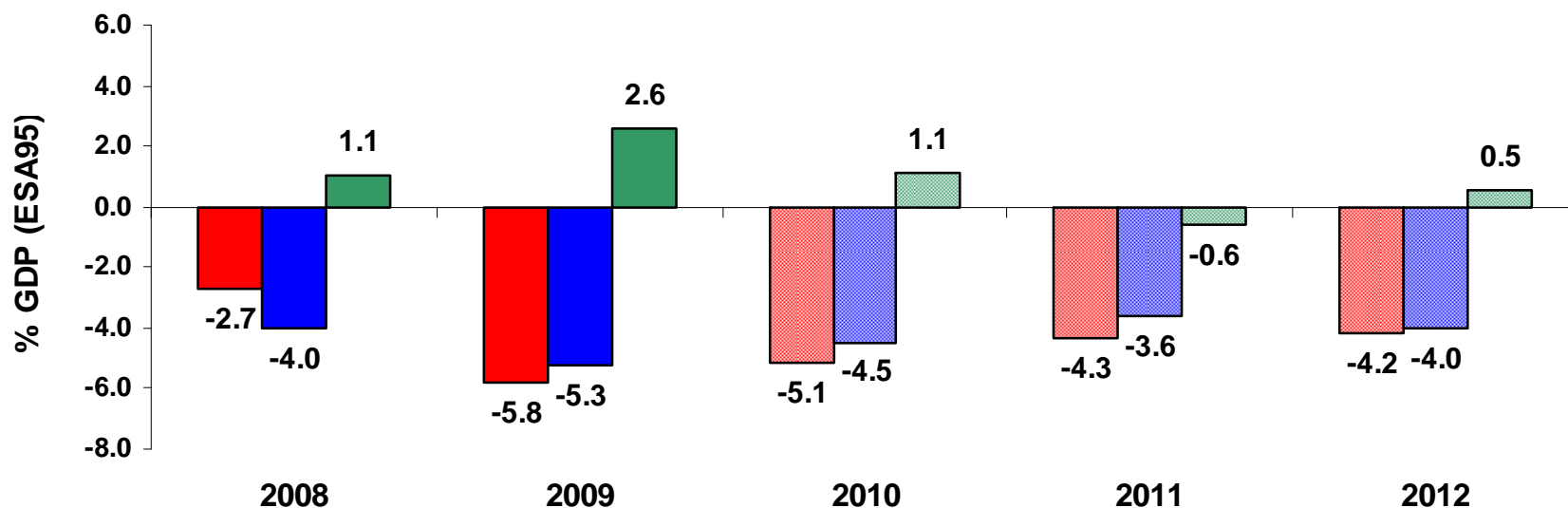


Imports Growth
(y/y, in %)



- All major demand components will slow down in 2011.

Public Budgets

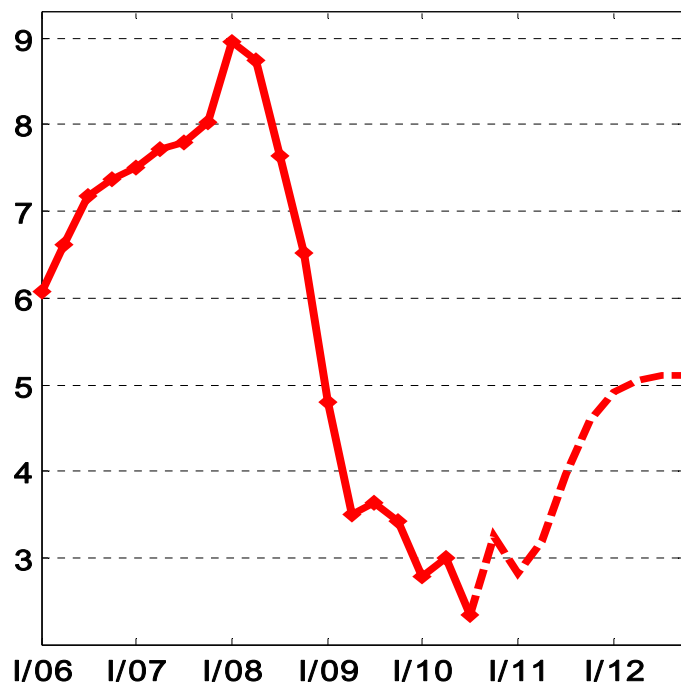


■ Public budget deficit ■ Structural deficit (EC) ■ Real government consumption (y-o-y %)

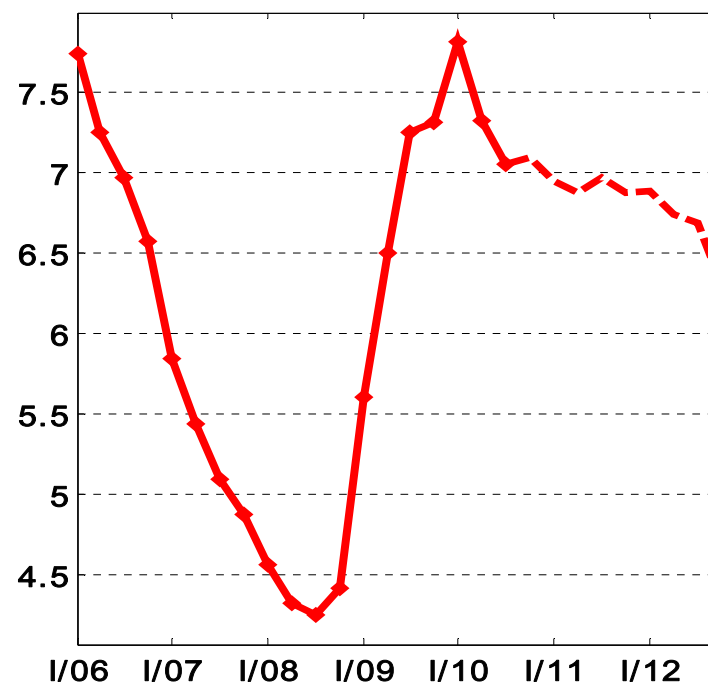
- The forecast still expects a decline of public budget deficits toward 4% of GDP due to fiscal consolidation.

Labour Market Forecast

Nominal wage growth in business sector
(y-o-y, in %, s.a.)

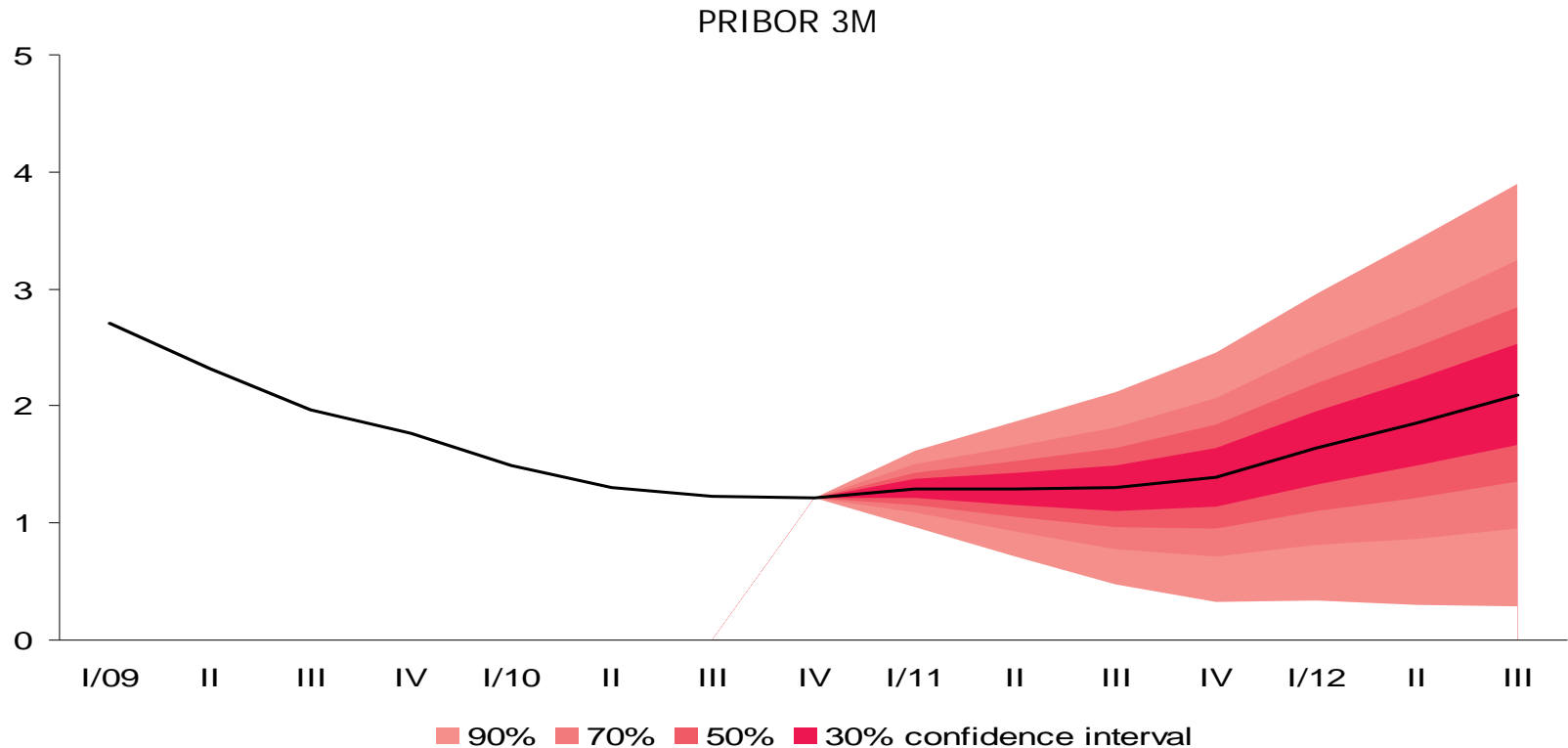


General unemployment rate (ILO)
(in %, s.a.)



- The private sector wage growth will start to pick up.
- Unemployment will fall only gradually until 2H 2012.

Interest Rate Forecast

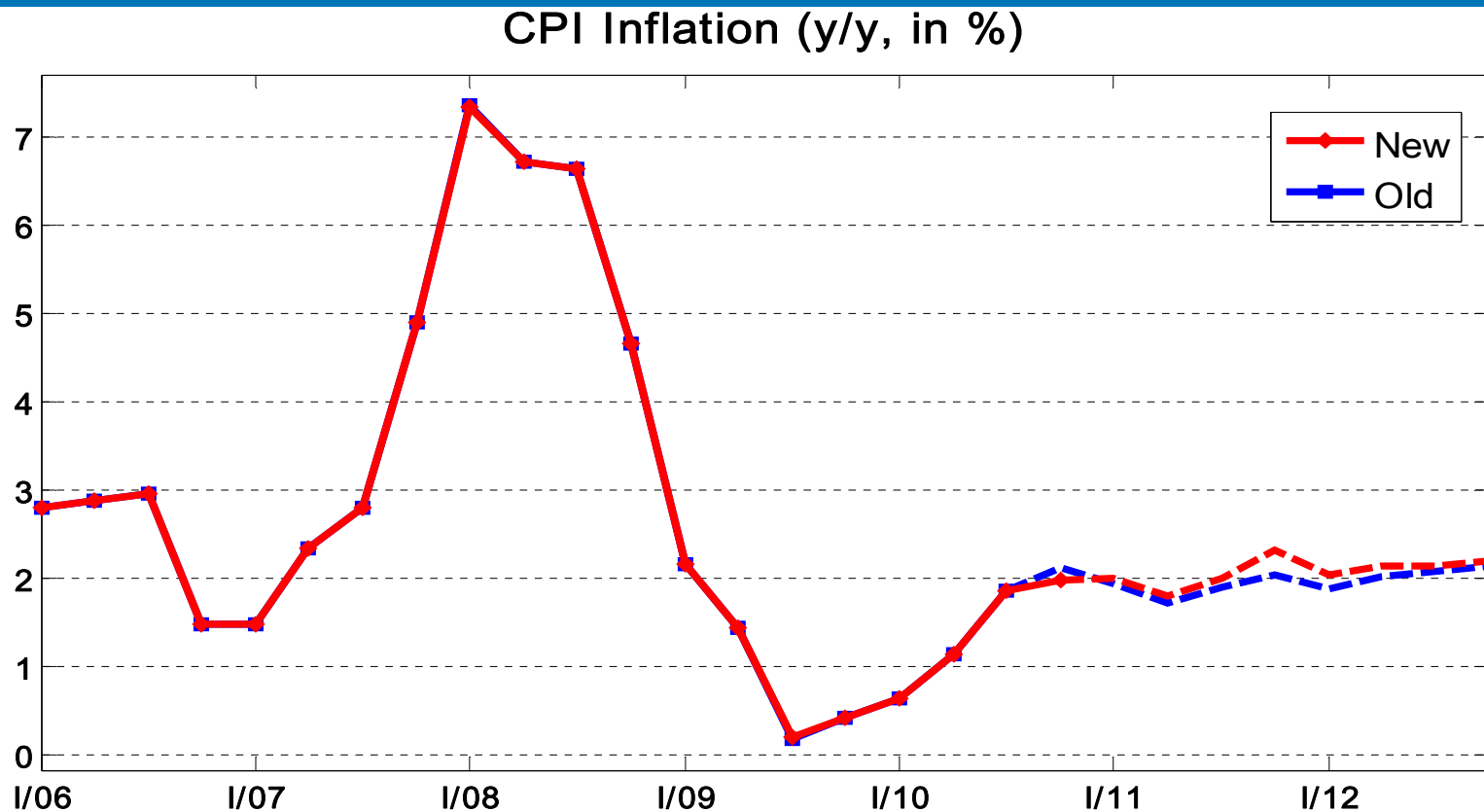


- Stability of market interest rates close to their current levels initially, followed by a gradual rise in rates as from the end of 2011.

Summary of the Comparison with Previous Forecast

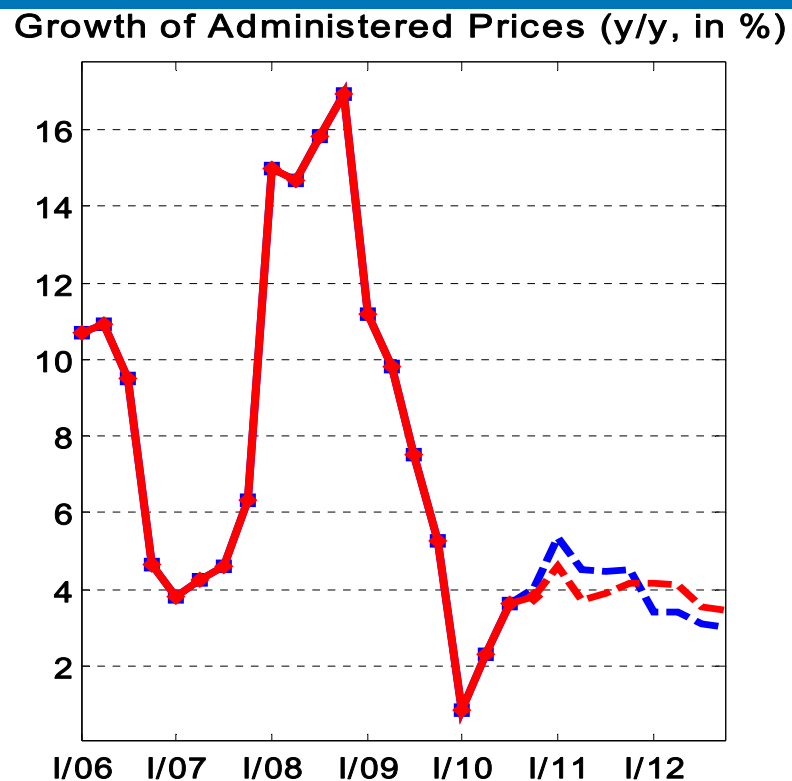
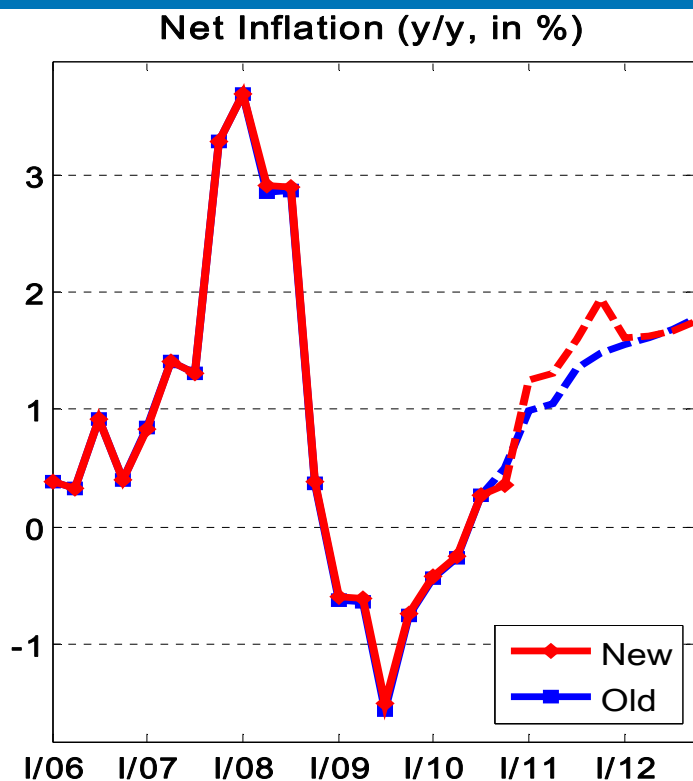
- The overall change in inflation forecast is small.
- Slightly higher net inflation vs. lower regulated price growth in 2011.
- The GDP forecast increased both for 2011 and 2012.
- The expected exchange rate and wage growth change only marginally.
- The interest rates start to grow somewhat sooner.

Comparison with Previous Inflation Forecast (i)



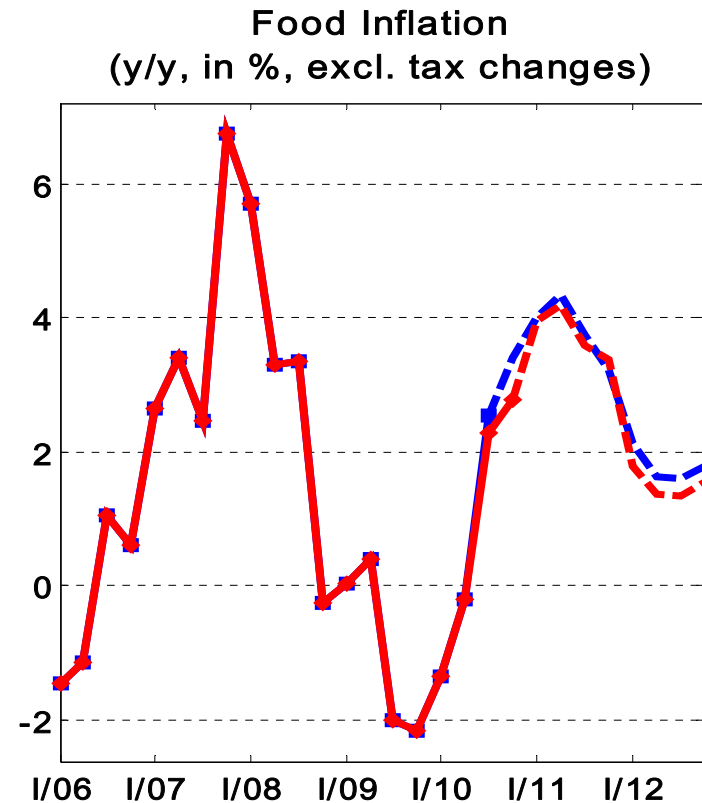
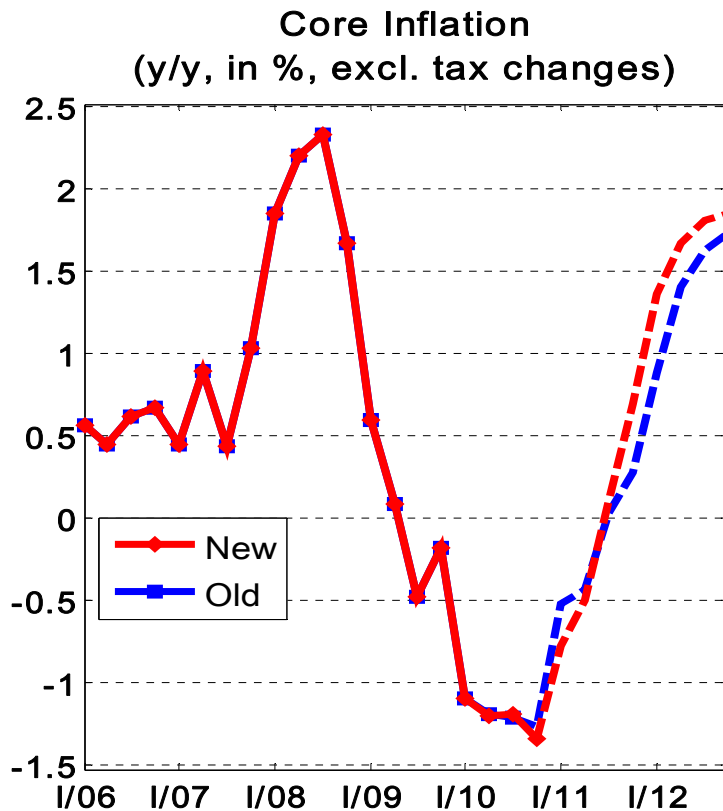
- The change in inflation forecast is small.

Comparison with Previous Inflation Forecast (ii)



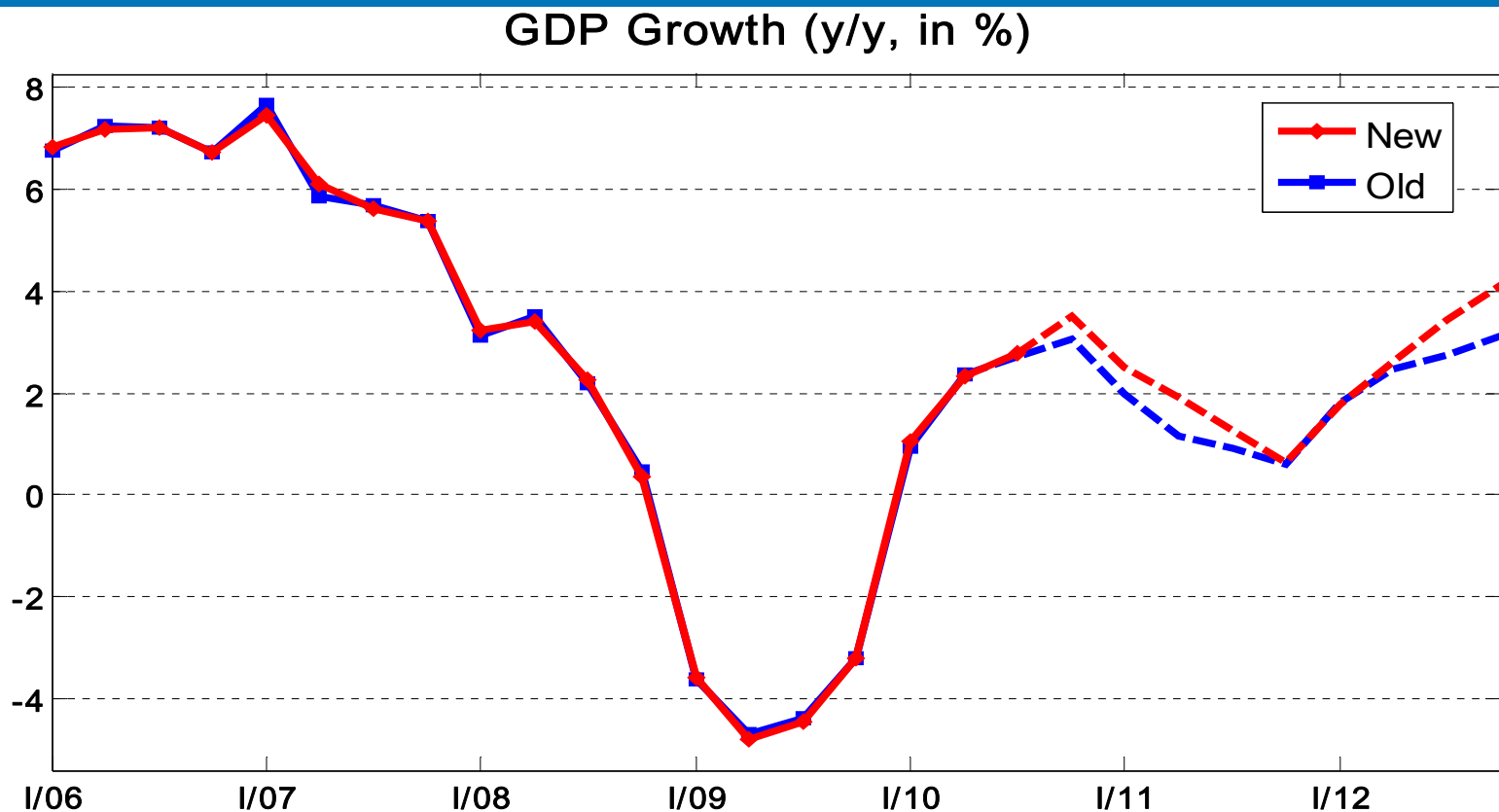
- Higher net inflation forecast due to commodity prices.
- Lower growth of administered prices (electricity).

Comparison with Previous Inflation Forecast (iii)



- The forecasts of core inflation and food prices change only marginally.

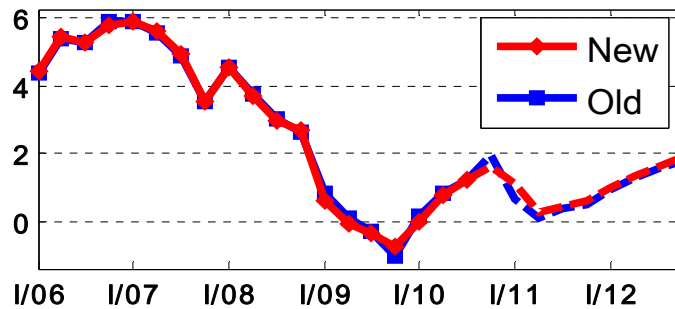
Comparison with Previous GDP Forecast (i)



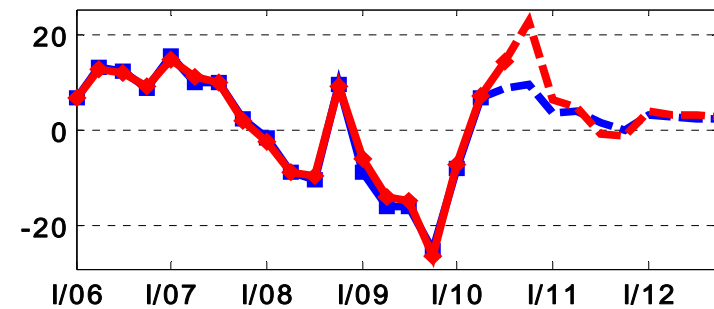
- The y/y GDP outlook increases both for 2011 and 2012, mainly due to higher foreign demand.

Comparison with Previous Aggregate Demand Forecast

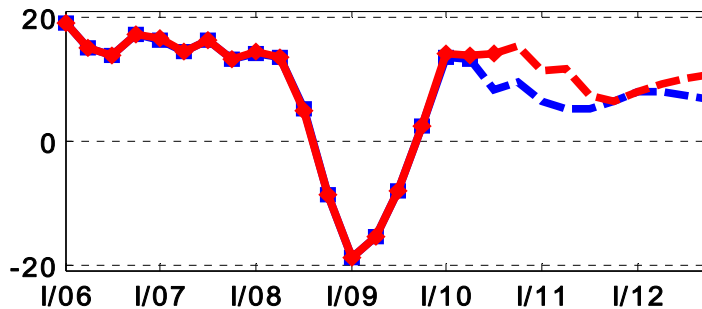
Household Consumption Growth
(y/y, in %)



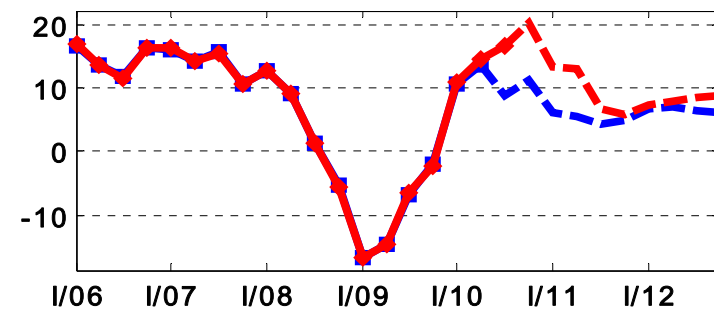
Investments Growth
(y/y, in %)



Exports Growth
(y/y, in %)



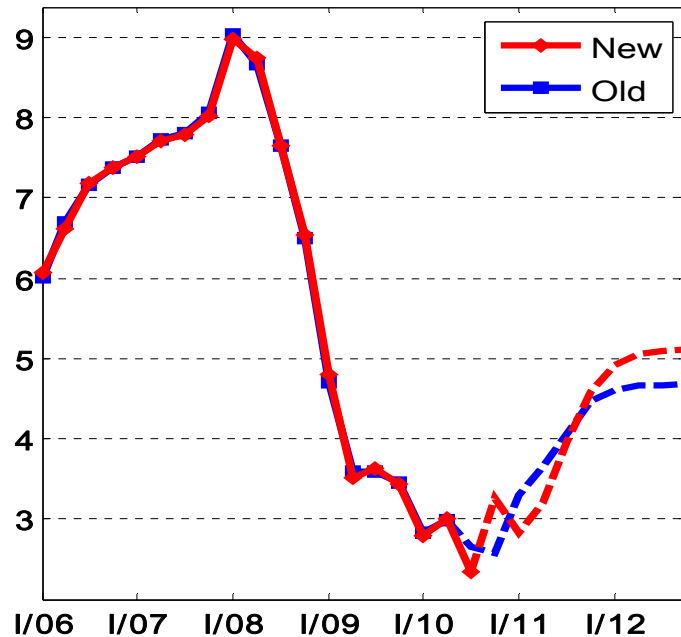
Imports Growth
(y/y, in %)



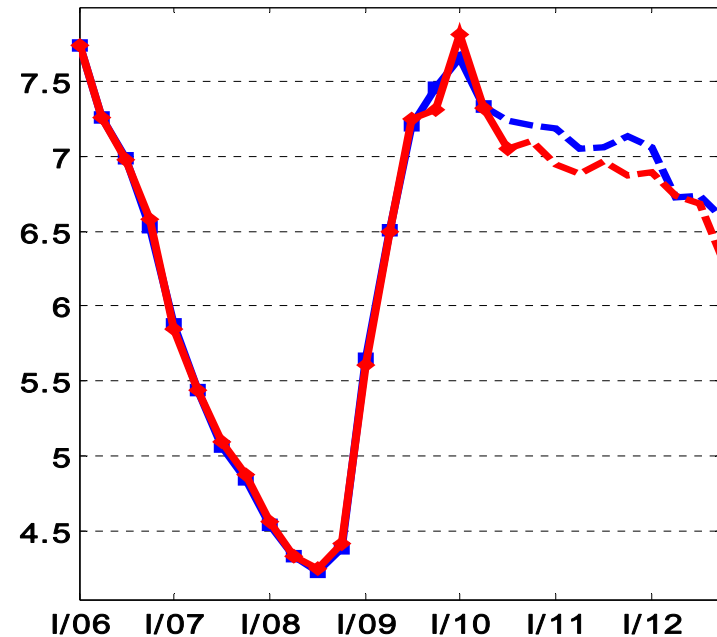
- Higher investment, import and export growth in the near term. Consumption forecast almost unchanged.

Comparison with Previous Labour Market Forecast

Nominal wage growth in business sector
(y-o-y, in %, s.a.)

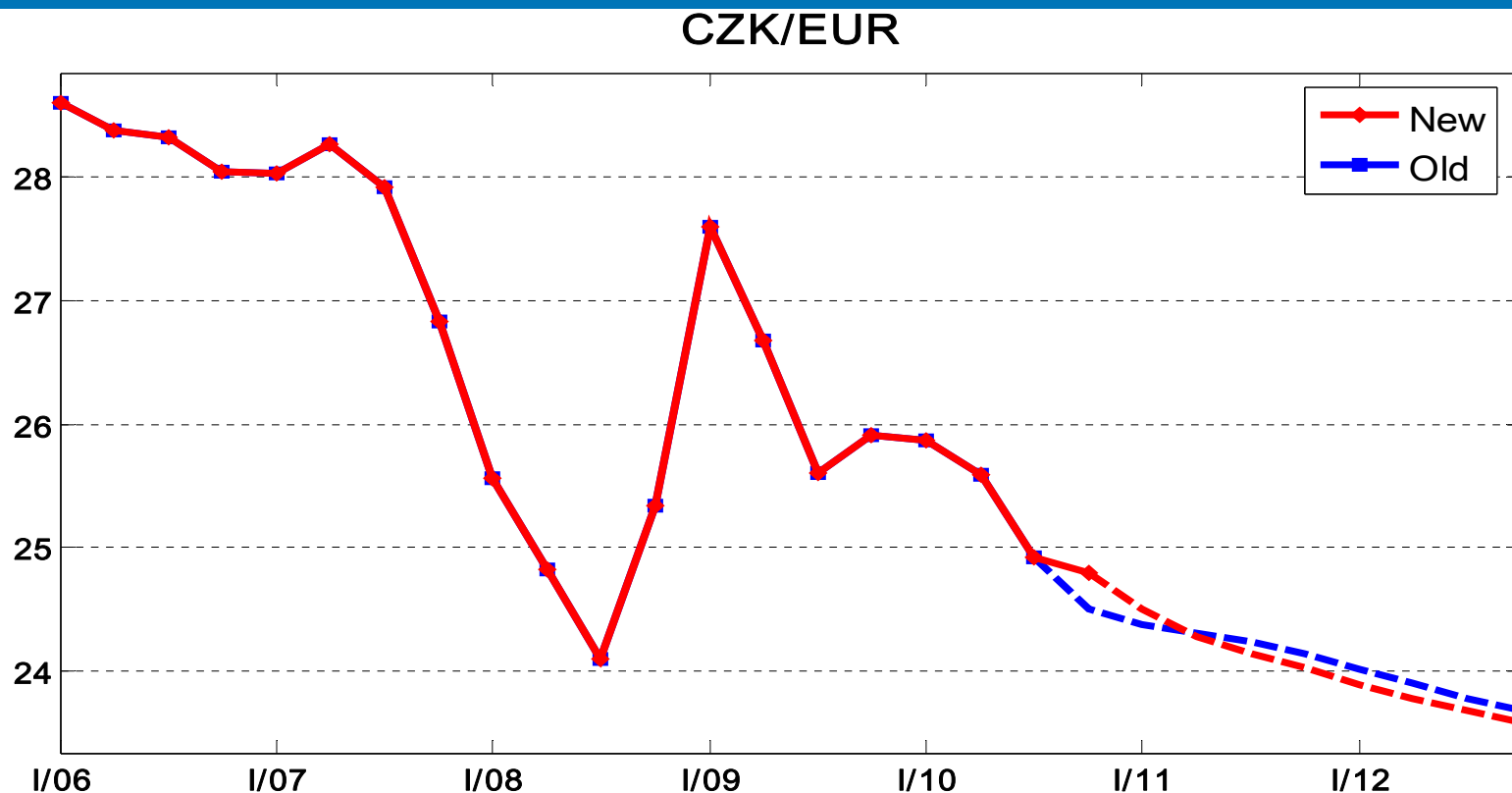


General unemployment rate (ILO)
(in %, s.a.)



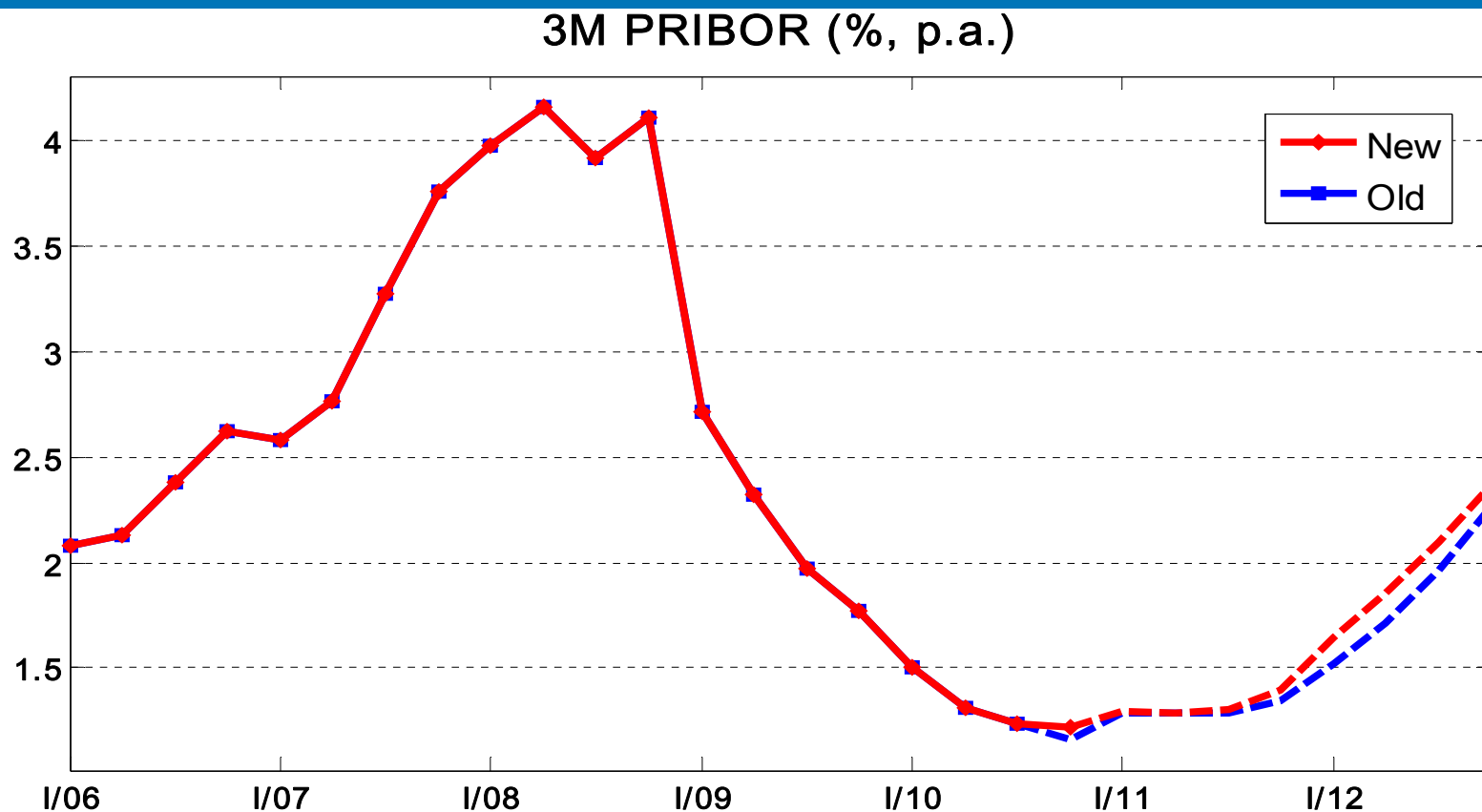
- Changes in the labour market forecast reflect lower observed wage growth and higher GDP outlook, but overall are quite small.

Comparison with the Previous Exchange Rate Forecast



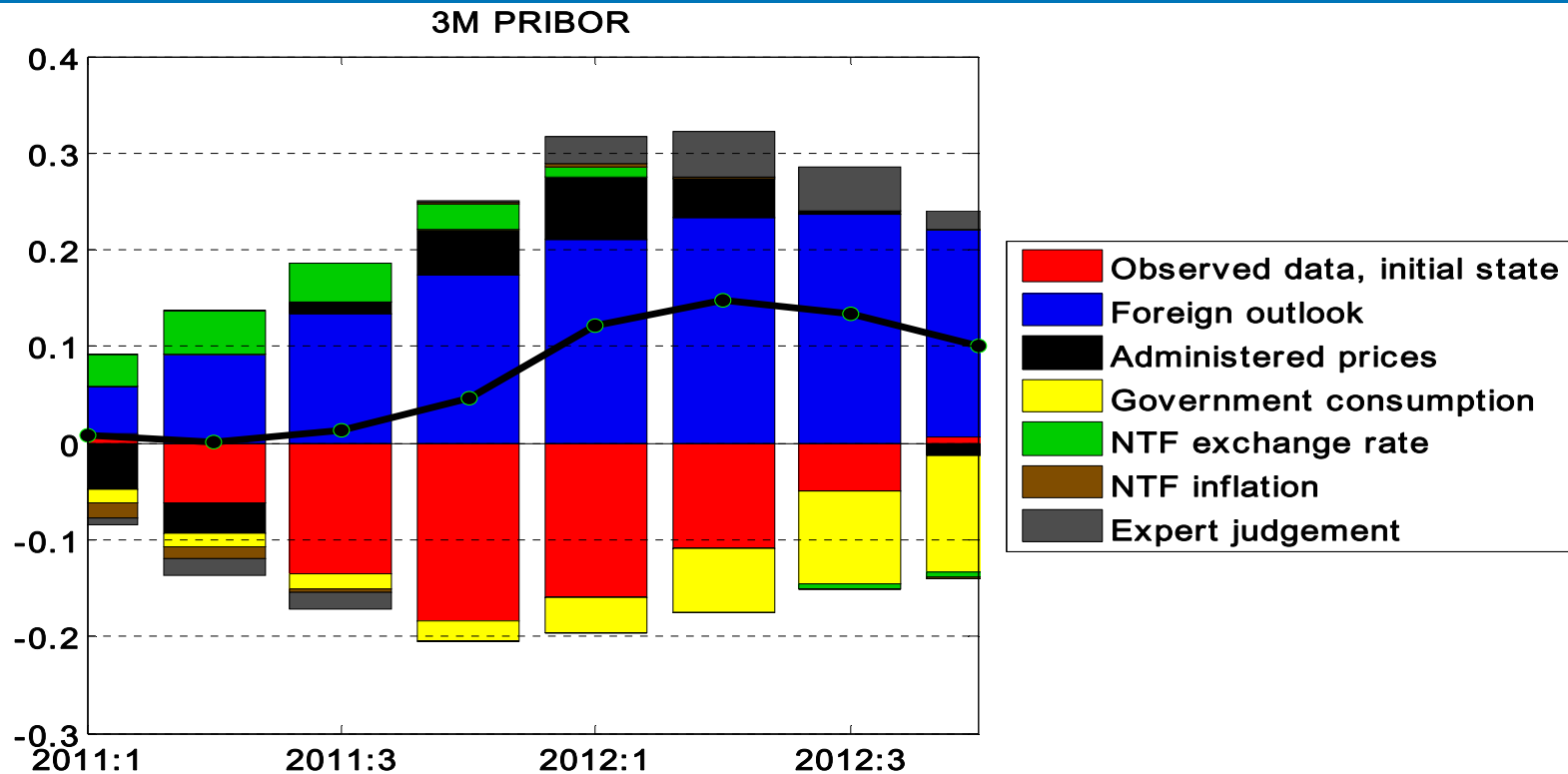
- The exchange rate path is similar to the previous forecast.

Comparison with the Previous Interest Rate Forecast



- The interest rate starts to increase slightly sooner than in the previous forecast.

Interest Rate Forecast Change Decomposition

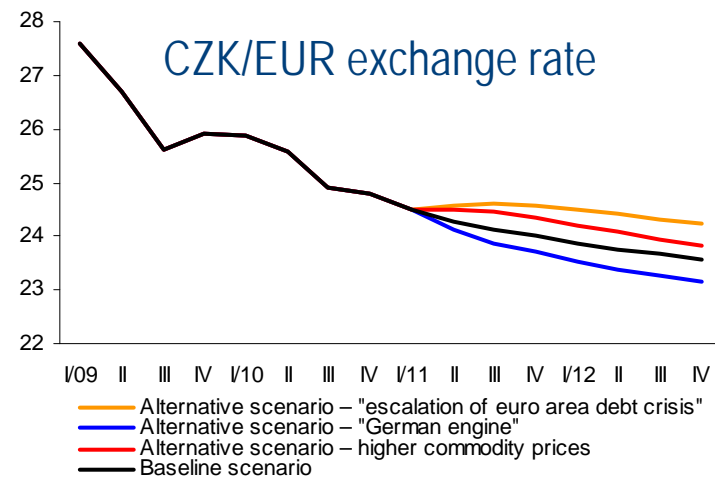
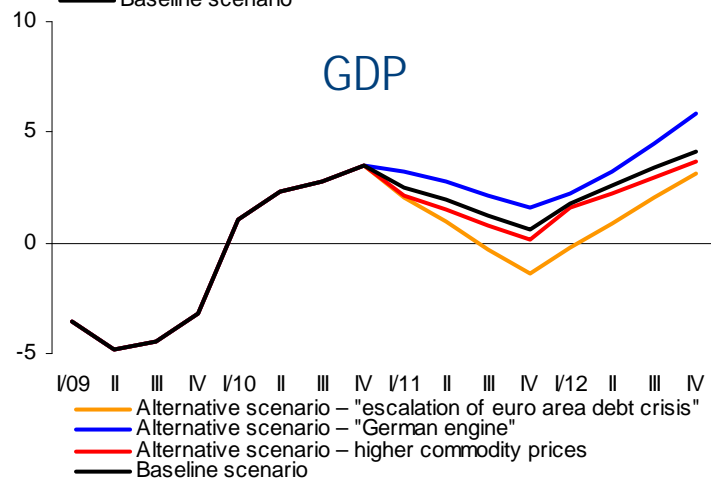
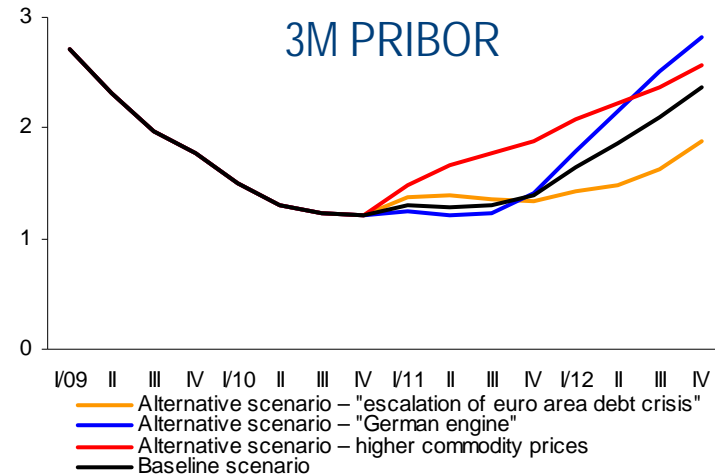
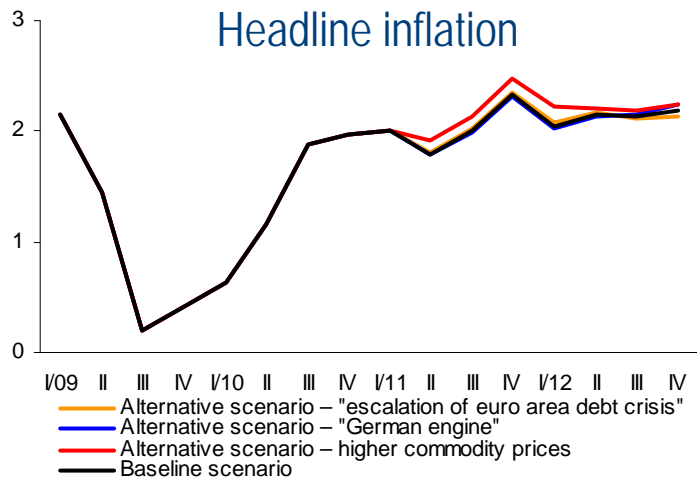


- The upward effect of external outlook starts to dominate as from the end of 2011 .

Alternative scenarios

- Alternative scenarios reflect the high uncertainty concerning the external economic outlook.
- Full-fledged simulations of alternative developments abroad (NiGEM) and their impact on the domestic economy.
 - A rise in global commodity price indexes (20 % for 3Ys)
 - “German engine” scenario (higher EA growth by 0.5 p.p.)
 - Escalation of Euro area debt crisis (lower EA growth by 1 p.p.)

Alternative scenarios





Thank you for your attention

www.cnb.cz

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