2004

INFLATION REPORT JULY/2004

CNB CZECH NATIONAL BANK

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ABBREVIATIONS USED

CNB	Czech National Bank
CPI	consumer price index
CZK	Czech koruna
CZSO	Czech Statistical Office
ECB	European Central Bank
ESCB	European System of Central Banks
EU	European Union
EUR	euro
FDI	foreign direct investment
FRA	forward rate agreement
GDP	gross domestic product
HICP	Harmonised index of consumer prices
IPI	Industrial production index
IRS	interest rate swap
LFS	Labour Force Survey
LIBOR	London Interbank Offered Rate
M1	a monetary aggregate (see section III.1.1.)
M2	a monetary aggregate (see section III.1.1.)
MLSA	Ministry of Labour and Social Affairs
O/N	overnight
PPI	producer price index
PRIBID 1W	Prague Interbank Bid Rate, one-week
(1M, 1Y)	(one-month, one-year)
PRIBOR	Prague Interbank Offered Rate
repo rate	repurchase agreement rate
USD	US dollar
VAT	value added tax

FOREWORD

In 1998, the Czech National Bank switched to direct targeting of inflation. In the inflation targeting regime, the central bank's communication with the public plays a significant role. One of the core elements of this communication is the regular publishing of Inflation Reports. In these pivotal documents the central bank provides information on monetary and economic developments in the previous quarter and on the reasons for the Bank Board's monetary policy measures. The Inflation Report also acquaints readers with the view of the Czech National Bank regarding the current position of the economy in the business cycle and its future development. The inflation forecast and the assumptions underlying it are published with the aim of making monetary policy transparent, comprehensible, predictable and therefore reliable. The Czech National Bank is convinced that reliable monetary policy effectively influences inflation expectations and minimises the costs of maintaining price stability. Maintaining price stability is the Czech National Bank's primary objective.

This Inflation Report was approved by the CNB Bank Board on 5 August 2004. As the Czech Republic became a Member State of the European Union and the Czech National Bank a member of the European System of Central Banks (ESCB) on 1 May 2004, the Annex to this Report gives an account of the Czech National Bank's current involvement in the activities of the ESCB.

This Inflation Report is also available at http://www.cnb.cz/. Unless stated otherwise, the sources of the data presented in this Inflation Report are the CZSO or the CNB.

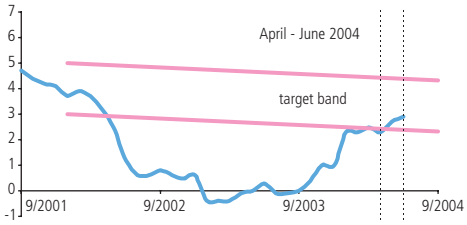
I. SUMMARY

Table I.1
INFLATION ROSE SOMEWHAT IN 2004 Q2
(annual percentage figures unless otherwise indicated)

	3/04	4/04	5/04	6/04
Consumer price inflation	2.5	2.3	2.7	2.9
Industrial producer price inflation	2.1	3.7	4.9	6.2
Money supply growth (M2)	7.7	8.3	9.0	x
3M PRIBOR[a)]	2.1	2.1	2.2	2.3
Nominal CZK/EUR exchange rate[b)]	32.98	32.51	31.97	31.61
State budget balance since January incl. SFAOs[b)], CZK bn	-7.8	-38.1	-45.4	-49.7
GDP growth at constant prices[c)]	3.1			x
Unemployment rate[b)]	10.7	10.2	9.9	9.9

a) average for the month
b) end-of-month position
c) figure for the quarter ending with the given month

Chart I.1
INFLATION WAS CLOSE TO THE LOWER BOUNDARY OF THE TARGET BAND IN 2004 Q2
(annual consumer price inflation, percentages)



The slight pick-up in annual consumer price inflation during 2004 Q2 took inflation back into the target band for the first time in around two years (see Chart I.1). The Czech economy grew at a rate of around 3% in 2004 Q1, the same as during 2003. Unemployment and wages continued to be determined primarily by a persisting excess of labour supply over demand of employers.

Inflation continued to edge up in 2004 Q2. After slowing slightly to 2.3% in April, annual consumer price inflation picked up pace again in the remaining months of Q2, gradually approaching the 3% level (2.7% in May and 2.9% in June). This pick-up in inflation was mainly due to a sharp increase in fuel prices, reflecting rising oil prices on world markets and continuing tax changes. Besides the two-way VAT changes, the rate of duty on tobacco products, which was increased in January, started to affect prices of these goods. Unlike in the previous quarter, food prices did not contribute to the rise in consumer price inflation.

On 1 May, the Czech Republic became a Member State of the European Union. Although this was in many respects a major event for the Czech Republic, the CNB was not expecting any great shock to inflation. The aforementioned inflation figures in Q2 confirmed that price stability had not been endangered by the Czech Republic's accession. In connection with accession, the annex to this Report briefly describes the CNB's integration into the activities of the European System of Central Banks.

In 2004 Q1, the Czech economy grew at the same rate as in 2003 as a whole. The growth continued to be driven by domestic demand, and in particular by fast-growing fixed investment. Household consumption was only in second place by size of contribution, as in the previous quarter. The growth contribution of government consumption was negative, as was that of the external sector. Net exports worsened mainly because of the fast growth in investment, which in the Czech economy is satisfied to a large extent by imports. The rise in imports was partly offset by faster export growth, aided in particular by a continuing external demand recovery and year-on-year depreciation of the koruna's exchange rate against the euro.

The developments on the labour market in 2004 Q2 continued to be characterised by an excess of labour supply over employers' demand for labour. However, the imbalance has eased somewhat this year, as evidenced by the fact that the decline in employment stopped deepening in Q1 and the unemployment rate fell just short of the ten percentage level in Q2. Although the current situation on the labour market is limiting the room for growth in business sector wages, their growth rate (especially of nominal wages) picked up in Q1. This chiefly reflected corporations' generally favourable performance, which allowed bonuses to be paid, as well as a higher number of hours of work.

The balance of payments was dominated in 2004 Q1 by the current account deficit, which roughly doubled year on year, mainly because of growing transfers of earnings abroad. The net inflow of capital declined to roughly one tenth of the level a year earlier, reflecting a sizeable outflow of banking sector funds. These facts also fed through in part to a modest depreciation of the koruna's exchange rate against the euro, which during Q2 switched to gradual appreciation. The koruna's exchange rate against the dollar fluctuated during the first half of the year. The differential evolution of the koruna-euro and koruna-dollar rates was due to movements in the euro-dollar rate.

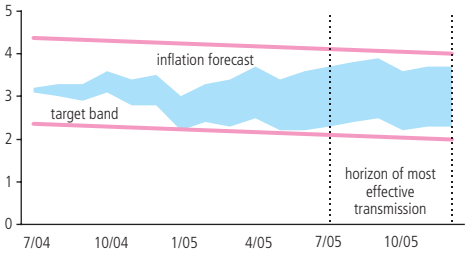
The monetary policy decision-making of the CNB Bank Board in 2004 Q2 was based on the inflation forecast discussed by the Board at its meeting on 29 April 2004 and

published in the April Inflation Report. Given the monetary policy transmission lag, the Board focused on hitting the inflation target in April–September 2005. According to the forecast, inflation should be close to the centre of the target band in this period. Consistent with the forecast was a gradual rise in interest rates at the two-year horizon.

The Bank Board did not increase monetary policy rates at the end of April as indicated by the forecast. This decision was based on a downward review of the risks of the forecast and uncertainties regarding its fulfilment in the areas of both inflation and economic growth. For similar reasons, the Bank Board also left monetary policy interest rates unchanged at the end of May. At its meeting at the end of June, the Board decided by a majority vote to raise interest rates by 0.25 percentage point with effect from 25 June.

As usual, section IV of this Inflation Report presents the CNB's new forecast. As in April, the forecast is for a pick-up in economic growth to around 4% in the course of 2004. The GDP growth should result in fairly rapid closure of the negative output gap in 2004 H2 and a subsequent gradual shift to positive values in 2005. Economic activity should be driven mainly by private investment and exports. According to the forecast, the exceeding of the economy's potential will lead to a resurgence of demand-pull inflationary pressures, particularly during 2005. The demand-pull effects will bring inflation close to the centre of the inflation target in 2005 H2. Consistent with the July forecast and its assumptions is a moderately rising path of short-term interest rates, which is, however, slightly lower than in the April forecast.

Chart I.2
THE INFLATION FORECAST IS AT THE CENTRE OF THE TARGET BAND AT THE HORIZON OF MOST EFFECTIVE TRANSMISSION
(annual consumer price inflation, percentages)



II. INFLATION DEVELOPMENTS

Chart II.1
THE PICK-UP IN ANNUAL CONSUMER PRICE INFLATION CONTINUED INTO 2004 Q2
(percentages)

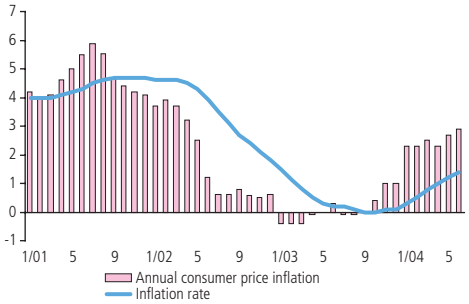
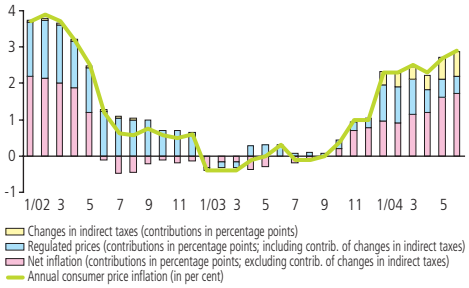


Table II.1
ITEMS WITH RISING PRICES PREDOMINATED IN THE CONSUMER BASKET
(annual percentage changes)

	12/03	1/04	2/04	3/04	4/04	5/04	6/04
Consumer prices	1.0	2.3	2.3	2.5	2.3	2.7	2.9
Food and non-alcoholic beverages	3.5	4.2	4.2	4.6	4.7	3.8	2.8
Alcoholic beverages and tobacco	0.7	0.8	0.8	0.9	1.6	3.1	3.9
Clothing and footwear	-4.6	-4.8	-4.8	-4.4	-4.6	-4.4	-4.1
Housing, water, electricity, gas and other fuels	1.9	4.2	4.2	4.2	2.9	2.4	2.5
Furnishings, household equipment and routine maintenance of the house	-2.0	-2.0	-2.1	-2.0	-1.8	-2.1	-1.8
Health	3.2	2.5	2.5	2.3	2.2	3.4	3.7
Transport	-0.5	1.1	0.6	0.9	1.2	3.5	3.7
Communications	-0.9	15.1	13.0	13.1	12.8	13	13.0
Recreation and culture	-1.0	-1.0	-0.8	-0.8	-0.6	0.4	2.0
Education	0.6	0.8	1.1	0.9	0.9	1.3	1.1
Hotels and restaurants	1.9	2.4	2.4	2.7	2.8	6.8	7.2
Miscellaneous goods and services	2.9	3.0	3.2	3.6	3.5	4.6	5.0

Chart II.2
MARKET PRICES (= NET INFLATION) AND CHANGES TO INDIRECT TAXES CONTRIBUTED TO THE RISE IN INFLATION IN 2004 Q2



II.1 PAST INFLATION DEVELOPMENTS

Inflation[1] increased further in 2004 Q2. Compared to the end of the previous quarter, it rose by 0.4 percentage point to 2.9% in June, the highest figure in two years.[2] The inflation rate[3] rose to 1.4% at the close of Q2. A continuing upturn in annual consumer prices was recorded for most categories of the consumer basket. Only in two categories did prices continue falling year on year (see Table II.1).

As in the previous quarter, the pick-up in annual consumer price inflation in 2004 Q2 was linked chiefly with extraordinary factors, most notably the further adjustments made to VAT on some services and goods with effect from 1 May 2004. Unlike in 2004 Q1, these changes were two-way in nature, since on some items VAT was increased from 5% to 19% while on a number of others it was cut from 22% to 19%. Actual inflation confirmed that these adjustments led to a rise in consumer prices overall. Inflation was also partly affected – with a lag – by the January 2004 changes to indirect taxes. Another more or less extraordinary factor was a sharp increase in oil prices on world markets, which passed through into fuel prices. Food prices ceased to contribute to the rise in consumer price inflation in 2004 Q2. Their faster growth at the beginning of the year had been associated in particular with rapid growth in agricultural producer prices.

Other inflationary factors again remained less significant in 2004 Q2. The upswing in prices of imported inputs ongoing since mid-2003 continued into Q2, again feeding through – with a lag – into industrial producer prices. However, prices grew faster in only a limited number of manufacturing industries directly engaged in processing imported raw materials whose prices recorded very rapid growth on world markets (besides oil primarily metals). In most other manufacturing industries, producer prices continued growing only modestly or even declined year on year. The gradual upswing in prices of imported inputs hence did not feed through into producer prices and on into consumer prices to any greater or wider extent. The continuing relatively fast year-on-year rise in agricultural producer prices was not fully reflected in domestic prices either.

Conditions on the demand side and on the retail market continued to prevent any greater pass-through of the rising input prices into producer and consumer prices. The fairly steady growth in consumer demand continued, but the economy remained below potential output. In addition, competition on the retail market remained strong, bolstered by the entry of new retailers in the hypermarket segment trying to gain market share. As in previous quarters, producers responded to the tough competitive environment by rationalising employment in order to cut their personnel costs relative to output. In both industry and construction, consequently, there were no wage-cost pressures on inflation. Favourable terms of trade also created some room for offsetting the rise in prices of imported inputs.

These inflationary factors affected market prices, as measured by net inflation.[4] The increase in net inflation by 0.7 percentage point to 2.1% in June compared to the end of 2004 Q1 was largely due to a year-on-year rise in fuel prices in response to the sharp

1 Measured by annual growth in consumer prices.

2 Since 2002 Q2.

3 The inflation rate expressed as the increase in the average consumer price index (basic) for the last 12 months relative to the average for the previous 12 months.

4 Net inflation = the increase in the consumer price index net of regulated prices and adjusted for other administrative measures.

increase in oil prices on world markets. In March fuel prices had still been declining year on year, whereas in June they recorded 14.1% growth. The VAT changes chiefly affected the nontradables segment (excluding items with regulated prices), which consists mainly of services. The regrading of some services – especially restaurant and personal services[5] – from the reduced 5% rate to the new 19% basic rate in May had a major effect on inflation in this category. However, inflation in this segment was lower than expected (5.9% year on year in June), most probably because of demand-side factors and greater competition in some fields (see Chart II.3).

Conversely, prices of other tradable commodities[6], which are affected chiefly by external conditions, continued to display an annual decline in 2004 Q2. The modest deepening of their annual decline was associated with the May reduction of the basic VAT rate from 22% to 19%. This step affected regulated prices more significantly. Whereas market commodities and services generally saw a lower rise in prices than would correspond to the VAT increase and, conversely, the decrease in prices was lower than originally expected, in the case of regulated items the VAT reduction fed through into electricity, gas and public telecommunication services prices to the full extent. Annual growth in regulated prices in 2004 Q2 thus slackened to 2.4%. The accumulated effect of the lowered VAT rate and the April cut in gas prices fostered a slowdown in housing prices (see Table II.1).

In 2004, consumer prices were also affected by the lagged impacts on tobacco product prices of the January 2004 changes to excise duties. Stocks of tobacco products stamped with prices valid prior to the January rise in excise duties were still being sold in 2004 Q1, as there were no time limits on such sales. Compared to the end of 2004 Q1, these prices rose by 3 percentage points year on year in Q2 (to 3.9% in June). Conversely, growth in prices of food and non-alcoholic beverages slackened in the course of 2004 Q2 (from 4.6% in March to 2.8% in June year on year). This change in trend was connected not only with a larger seasonal decline in the prices of some volatile items in June, but also with several other effects. Relatively fast agricultural producer prices growth was not fully reflected in food prices, as it concerned only a limited number of crop commodities. These commodities usually affect food prices indirectly and their weight in the agricultural producer price index is higher than in food prices. The effect of the rapidly rising producer prices of the aforementioned commodities on food prices was partly attenuated by a reduction in margins in manufacturing.

The overall and structural evolution of consumer price inflation in 2004 Q2 confirmed that the main factors underlying the increasing annual inflation were fast-growing oil prices on world markets and the changes in indirect tax rates. Overall, the contribution of the two-way tax changes to the rise in inflation was positive, although the response to these tax adjustments in market prices was generally smaller than would correspond to the change in tax rates. The changes to VAT rates at the start of May fostered an increase in prices primarily in services. According to the CNB's calculations, prices of nontradable commodities (chiefly services) thus continued to rise faster than tradable commodities (chiefly goods). In June they rose by 4.4% and 1.3% respectively year on year.

By international comparison, annual consumer price inflation in the Czech Republic as measured by the Harmonised Index of Consumer Prices (HICP) had until 2003 Q3 been

Chart II.3
WITHIN THE MARKET PRICES CATEGORY, PRICES OF FUELS AND SERVICES SHOWED THE STRONGEST ANNUAL PICK-UP IN GROWTH
(annual percentage changes, including VAT changes)

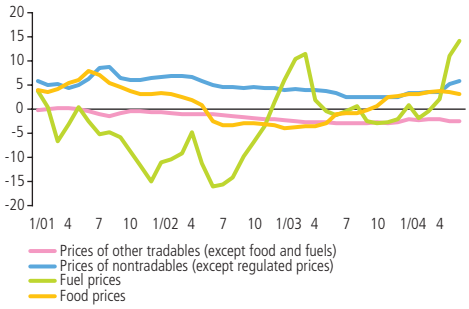


Chart II.4
THE LOWERING OF THE BASIC RATE OF VAT ACCOUNTED FOR MUCH OF THE SLOWDOWN IN ANNUAL REGULATED PRICE INFLATION
(percentages)

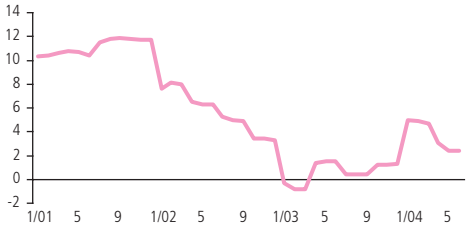


Chart II.5
ANNUAL FOOD PRICE INFLATION EASED IN 2004 Q2
(annual percentage changes)

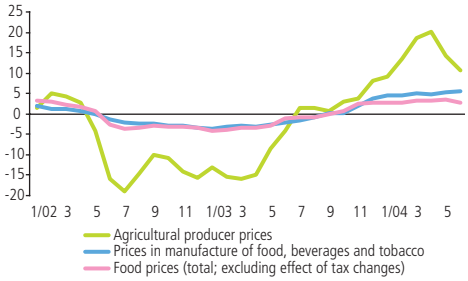
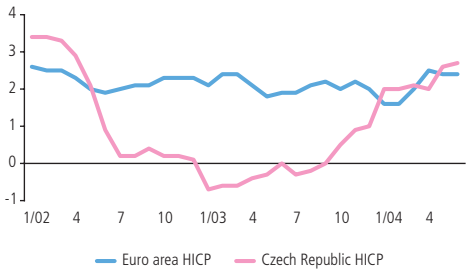


Chart II.6
CONSUMER PRICE INFLATION IN THE CZECH REPUBLIC WAS JUST ABOVE THE EURO AREA INFLATION LEVEL IN JUNE
(annual percentage changes)



5 This group includes, for example, hairdressing, cleaning, repairs and suchlike.

6 Excluding food and fuels.

fluctuating below the inflation level in the eurozone. The gradual rise in the Czech HICP ongoing since 2003 Q3 resulted in a slightly higher value (2.7%) being recorded in June 2004 than in the euro area countries.

II.2 FULFILMENT OF THE INFLATION TARGET

Actual inflation returned to the CNB's target band in 2004 Q2 (see Chart I.1). This section of the Inflation Report briefly analyses the contribution of the CNB's monetary policy to this situation.

TABLE II.2
HEADLINE INFLATION IN 2004 Q2 WAS SLIGHTLY HIGHER THAN THE JANUARY 2003 FORECAST
(annual percentage changes, contributions in percentage points)

	January 2003 forecast	June 2004 outturn	Contribution to total difference in perc. points
Annual consumer price inflation	2.7	2.9	0.2
Breakdown into contributions:			
regulated prices	2.8	2.4	-0.07
indirect taxes	0.00	0.68	0.68
food prices, excluding changes to indirect taxes	2.8	2.7	-0.03
fuel prices, excluding changes to indirect taxes	-4.1	11.2	0.47
adjusted inflation excluding fuels, excluding changes to indirect taxes	3.1	1.4	-0.87

Changes to interest rates pass through into inflation most strongly with a lag of roughly 12 to 18 months. Accordingly, to assess the effect of monetary policy on the fulfilment of the inflation target in 2004 Q2, one needs to analyse retrospectively the forecasts, and the Bank Board's decisions based thereon, dating from around October 2002 to June 2003. For simplicity, the analysis of the accuracy of the CNB's forecast is limited here to a comparison of the forecast drawn up in January 2003, i.e. approximately in the middle of the aforementioned period, with inflation in June 2004 (see Table II.2).

The January 2003 forecast had indicated gradual closure of the negative output gap as a result of easier monetary conditions[7] and fiscal stimulus. Accordingly, inflation was to have risen to the lower boundary of the target band in June 2004 (see the January 2003 Inflation Report). The consumer price inflation outturn in June 2004 was slightly higher than this (by 0.2 percentage point). A more detailed look at the inflation structure reveals that fuel prices grew faster than forecasted and the contribution of indirect taxes was higher, too. By contrast, regulated prices and adjusted inflation excluding fuels grew more slowly than forecasted in January. Food prices developed in line with the January forecast.

TABLE II.3
THE DIFFERENT-THAN-FORECASTED STRUCTURE OF THE JUNE INFLATION WAS PARTLY DUE TO THE ANTI-INFLATIONARY EVOLUTION OF MOST EXTERNAL FACTORS

		I/2003	II/2003	III/2003	IV/2003	I/2004	II/2004
GDP in Germany	prediction	0.6	0.8	0.9	1.2	1.6	1.8
(annual perc. changes)	outturn	0.1	-0.3	-0.3	0.1	0.7	x
CPI in Germany	prediction	0.9	0.9	1.2	1.6	1.3	1.5
(annual perc. changes)	outturn	1.2	0.8	1.0	1.2	1.1	1.9
1Y EURIBOR	prediction	3.3	3.4	3.5	3.7	3.7	3.7
(percentages)	outturn	2.5	2.2	2.2	2.4	2.1	2.3
USD/EUR exchange rate	prediction	1.05	1.04	1.05	1.05	1.05	1.06
(levels)	outturn	1.07	1.14	1.12	1.19	1.25	1.20
Oil prices	prediction	26.6	24.9	23.9	22.8	22.1	22.1
(USD/barrel)	outturn	30.1	24.1	27.2	27.5	29.8	32.2

The difference in the structure of actual inflation from the January forecast can be put down to unexpectedly disinflationary exogenous factors lying partly or completely outside the purview of the CNB's monetary policy (weak external demand, low inflation abroad, the euro's appreciated exchange rate against the dollar, higher oil prices – see Table II.3), higher-than-expected indirect tax changes[8] and imperfections in the CNB's forecasting system.

Consistent with the January forecast was a slight decline in interest rates at the beginning of 2003, flat rates until the end of 2003 and a slight rise in 2004 H1. In reality, the decline in interest rates was sharper and longer lasting, as monetary policy interest rates were lowered by 0.75 percentage point in three steps in the period from January 2003 onwards. This notwithstanding, real interest rates developed in line with the forecast during 2003 thanks to the greater-than-forecasted decline in inflation. By comparison with the January forecast, the exchange rate effect was assessed as tighter. Although the koruna's nominal exchange rate was more depreciated than forecasted, a lowering of the estimated rate of equilibrium appreciation prevailed in evaluating the exchange rate effect on the economy. Overall, the monetary conditions were tighter by comparison with the January forecast.

Several revisions have been made to the forecasting system since the forecast was drawn up in January 2003. These revisions change the CNB's view on the functioning of the

7 An explanation of this term can be found in the box *Monetary Conditions* in the April 2004 Inflation Report.

8 The January forecast assumed zero changes to indirect taxes. The principle of incorporating administrative price changes into the CNB forecast only when they have been approved by the Czech Parliament, or when the Czech Republic becomes obliged to implement such changes under EU rules, was thus applied.

economy, thus playing a significant role in the assessment of the extent of fulfilment of the January forecast. Since January 2003, two major changes have been carried out: the aforementioned lowering of the estimated rate of equilibrium appreciation of the koruna's exchange rate in 2003, and a reduction in the expert view of the price rigidity of some items of the consumer basket.

The contradictory effects of these two revisions on fulfilment of the January forecast roughly offset each other. The changes to the modelling system did not have a major effect on the deviation of the June inflation from the January forecast. Based on the CNB's present knowledge of the functioning of the Czech economy, as captured in its forecasting system, the developments since the January forecast was drawn up can be briefly interpreted in the following way.

As a result of tighter monetary conditions in the key period (October 2002 – June 2003) and lower external demand, the output gap widened in 2003 instead of closing as forecasted, despite higher-than-expected GDP growth[9] (see Table II.4). This was reflected in lower-than-forecasted inflation throughout 2003. In 2004, the output gap changes trend and starts closing as a result of easier monetary conditions in 2003 H2. The closure of the output gap together with the indirect tax changes led to a rise in inflation in 2004 H1.

The inflation forecast is the primary source material for the Bank Board's decisions. Also of key importance for its decision-making is an assessment of the possible risks associated with this forecast by the board members. At the Board's meetings during the final quarter of 2002 (see the relevant minutes), the risks were perceived as slightly anti-inflationary. In 2003 Q1 they were seen as symmetrical to slightly inflationary, and in 2003 Q2 as strongly anti-inflationary. The Bank Board's overall anti-inflationary perception of the risks contributed to easier monetary policy and thus to the fulfilment of the inflation target in 2004 Q2.

Table II.4
TIGHTER MONETARY CONDITIONS LED TO A WIDENING OF THE OUTPUT GAP IN 2003

		I/2003	II/2003	III/2003	IV/2003	I/2004	II/2004
3M PRIBOR	prediction	2.5	2.6	2.6	2.6	2.8	2.9
(percentages)	outturn	2.5	2.4	2.1	2.1	2.1	2.2
CZK/EUR exchange rate	prediction	31.0	31.0	30.5	30.3	30.2	29.9
(levels)	outturn	31.6	31.5	32.2	32.1	32.9	32.1
GDP	prediction	2.2	2.5	3	3.7	3.3	3.5
(real. annual perc. changes)	outturn	2.8	2.9	3.4	3.3	3.1	x
Output gap	prediction	-2.1	-1.8	-1.7	-1.5	-1.4	-1.1
(percentages of GDP)	outturn*	-1.1	-1.3	-1.5	-1.8	-1.7	-1.2

*estimate based on the July 2004 forecast of the CNB

9 A more detailed explanation of this apparent paradox can be found in the Box: *Use of the output gap indicator at the CNB* in the October 2003 Inflation Report.

III. INFLATION FACTORS

Table III.1
THE PICK-UP IN ANNUAL M2 GROWTH WAS ACCOMPANIED BY DEMAND FOR NARROW MONEY AMID A SLIGHT SLOWDOWN IN QUASI MONEY GROWTH
(quarterly figures are averages, end of month, percentages)

	II/03	III/03	IV/03	I/04	4/04	5/04	Outstanding amount as a percentage of M2 5/04
M1	16.4	15.6	14.4	14.7	14.7	17.1	51.9
Currency in circulation	14.1	15.0	12.8	10.7	9.1	8.3	12.7
Overnight deposits	17.2	15.8	15.0	16.0	16.8	20.3	39.2
M2-M1 (quasi money)	-7.1	-3.3	-2.9	0.1	2.5	1.3	48.1
Deposits with agreed maturity	11.3	12.1	0.0	2.0	3.8	1.9	37.5
Dep. bills of exch. and other bonds	-13.5	8.1	6.8	38.5	52.2	40.3	6.7
Deposits redeemable at notice	-39.7	-33.7	-10.0	-5.0	-4.6	-3.4	9.9
Repurchase agreements	-55.8	-49.8	-36.5	-19.3	66.6	76.2	0.7
M2	3.0	5.3	5.2	7.0	8.3	9.0	100.0

Chart III.1
THE GROWTH RATES OF M1 AND HOUSEHOLD CONSUMPTION EXPENDITURE DID NOT ACCELERATE IN 2004 Q1
(annual percentage changes)

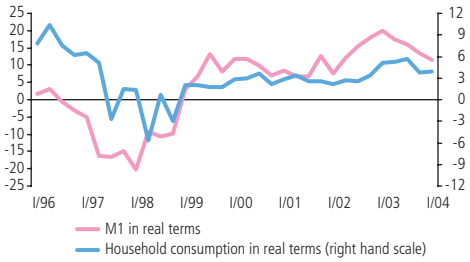


Chart III.2
ANNUAL GROWTH IN LOANS ACCELERATED
(percentages)

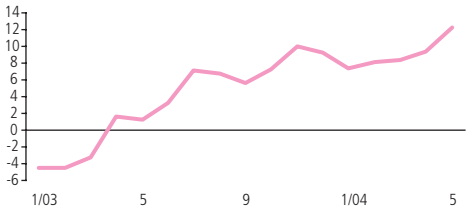


Table III.2
ANNUAL GROWTH IN LOANS TO NON-FINANCIAL CORPORATIONS INCREASED
(percentages)

	II/03	III/03	IV/03	I/04	4/04	5/04
Loans to non-financial corporations	-7.7	-4.5	-1.0	-1.0	0.7	3.7
Loans up to 1 year	-10.0	-6.3	-4.4	2.4	2.4	3.9
Loans over 1 year and up to 5 years	-12.6	-9.0	-1.4	-2.9	-2.0	2.8
Loans over 5 years	-0.5	1.3	3.9	-3.8	0.6	4.1

III.1 MONETARY DEVELOPMENTS

III.1.1 Money

Annual M2 growth increased to 9.0% in March–May 2004. The higher money growth ongoing since mid-2003 was in line with the expected upturn in economic growth. This trend was also confirmed by the annual growth rate[10] of M2 calculated on the basis of financial transactions according to ECB methodology. In March–May this growth rate rose by 1 percentage point to 9.5%

Within M2, the high demand for narrow money expressed by the monetary aggregate M1 persisted in March–May 2004. After stagnating in Q1 and in April 2004 its annual growth increased to 17.1% in May 2004. This showed up in overnight deposits of non-financial corporations. Around half of their growth was due to movement of money out of the nonmarketable securities (deposit bills of exchange) included in quasi money. The increase in the highly liquid money of non-financial corporations may be linked with transactions resulting from the investment recovery. Within M1, conversely, growth in households' overnight deposits was flat. At the same time, the annual cash growth rate declined, which was consistent with the unchanged growth rate of household consumption expenditure in 2004 Q1.

After picking up pace in Q1 and April 2004, annual quasi money growth slackened to 1.3% in May. This was reflected in lower growth in nonmarketable securities of non-financial corporations.

III.1.2 Credit

The growth rate of loans accelerated in March–May 2004. Their annual growth rose by 4.1 percentage points to 12.3% in the period under review (the annual growth rate calculated according to ECB methodology reaching 13.9% in May 2004). Loans to non-financial corporations and households both increased. A higher growth rate of loans was also recorded by non-monetary financial institutions, which include, *inter alia*, leasing and insurance companies. The growth in loans confirmed that the investment recovery ongoing since Q1 has a longer-term tendency.

After having recorded a gradual halting decline in 2003 and 2004 Q1, the growth rate of loans to non-financial corporations rose in April and May 2004. Annual growth in these loans was 3.7% in May 2004. This was linked with the economic growth and reflected the gradual upturn in effective demand for credit resulting from corporations' better financial condition. Rising output was recorded in 2004 Q1 by non-financial domestic and to an even greater extent by foreign-controlled corporations. Loans extended to domestic non-financial corporations rose by 7.5% in May 2004, whereas loans to foreign-controlled non-financial corporations fell by 4.8%, despite having recorded a halting decline in the previous period. These corporations also used their own internal funds to finance their economic activities, as evidenced by a slight rise in the share of equity in the liabilities of these corporations in 2004 Q1.

10 The annual money growth rate used for ECB monetary analyses is calculated from monthly transaction flows (i.e. differences between stocks of monetary aggregates) adjusted for exchange rate movements, reclassifications and other revaluations which are not a result of these transactions. The annual growth rate for the month is the product of the 12 coefficients of each previous month. According to the ECB, the main goal of using the aforementioned calculation method is to ensure more accurate comparability of monetary aggregates across individual periods.

Turning to the time structure of loans to non-financial corporations, loans of all maturities rose in March–May 2004. The share of medium-term and long-term investment loans (loans with a maturity of over one year) in short-term operating loans (loans with a maturity of up to one year) increased modestly in the period under review, this being in line with the recovery in investment activity in 2004 Q1.

The costs associated with borrowing, as expressed by the interest rate spread between the interest rate on loans extended to these corporations (i.e. external financing costs) and the 1Y PRIBOR (i.e. internal financing costs), are significant for future investment by non-financial corporations. The interest rate spread has been falling since 2003. This decline is consistent with the better financial condition of corporations. It may also reflect banks' greater willingness to lend or increased competition among banks.

Loans extended to households recorded buoyant growth in March–May 2004. Their annual growth rose by 2.3 percentage points in May 2004, to 31.6%. Housing loans accounted for most of this growth, despite showing a slight fall in April 2004. The annual growth rate of these loans reached 39.1% in May 2004. The main factors were persisting household demand for investment in property, stable growth in real disposable income and low interest rates. The interest rate on new housing loans extended to households declined by 0.3 percentage point to 5.1% in March–May 2004. Another significant factor was the supply of new products (e.g. American mortgages and mortgages for co-operative flats). The share of new housing loans in total new loans to households increased by 7.8 percentage points in March–May 2004, to 34%. This trend was visible for new housing loans with an initial rate fixation of over one and up to five years and of ten years or more.

The share of newly granted consumer credit and bank overdrafts in total new loans to households declined in March–May 2004. Annual growth in total consumer credit increased slightly in April 2004 and then flattened out. Given the minimal lag between borrowing and consuming, this trend was consistent with the flat annual consumption expenditure growth in 2004 Q1.

Despite falling slightly in 2004 Q1, the high annual growth rate of loans was reflected in a deteriorating financial balance[11] of households. There was a simultaneous gradual decrease in the gross savings rate. The growth in loans to households was reflected in the longer run in a rise in the ratio of the absolute volume of loans to gross disposable income. This ratio reached 17.2% in 2003. The ratio of absolute growth of loans and financial liabilities to gross disposable income decreased in 2004 Q1. A similar, albeit more intense, trend was recorded for households' financial assets. The ratio of household loans to deposits increased to 24.2% in 2004 Q1, the ratio for housing loans being 15.2% and that for consumer credit being 7.1%. The level of financial and non-financial assets is important as regards households' ability to repay loans in the event of an unexpected fall in gross disposable income or a rise in unemployment and interest rates. The ratio of household investment in real estate to gross disposable income had been increasing in the long term and has been flat since 2003. This trend may reflect, *inter alia*, the movement of property prices.

The ratio of interest expenses to gross disposable income in 2004 Q1 indicated a slight increase in households' debt load. This ratio rose from 1.8% in 2003 Q4 to 2.3% in 2004 Q1. Interest costs are currently low in relation to gross disposable income, but nevertheless suggest a rising debt burden on households. In the longer run, a potential negative effect

Chart III.3
THE SPREAD BETWEEN THE INTEREST RATE ON LOANS TO NON-FINANCIAL CORPORATIONS AND THE 1Y PRIBOR HAS BEEN FALLING SINCE 2003
(percentage points)

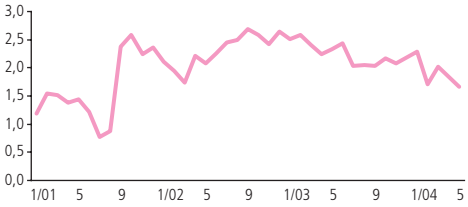


Chart III.4
THE ANNUAL GROWTH RATE OF HOUSING LOANS REMAINED BUOYANT
(percentages)

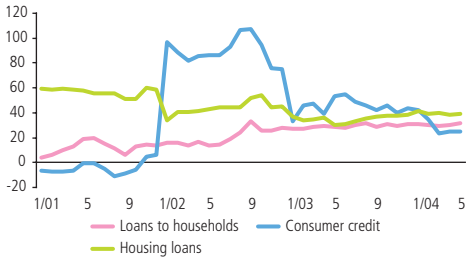
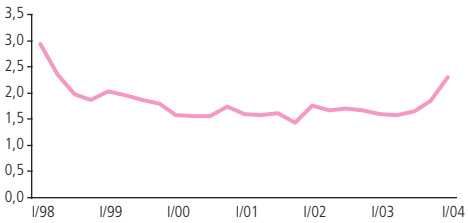


Chart III.5
THE FINANCIAL BALANCE OF HOUSEHOLDS DETERIORATED IN 2004 Q1
(percentages of gross disposable income)

Chart III.6
THE RATIO OF INTEREST EXPENSES TO GROSS DISPOSABLE INCOME INCREASED IN 2004 Q1
(percentages)



11 The financial balance of households (net saving) represents the difference between gross saving (gross disposable income minus consumption) and investment. As regards financial resources, it means the difference between households' financial assets and liabilities.

on the financial situation of households connected with a change in mortgage rate fixation cannot be excluded.

III.2 DEVELOPMENTS ON THE FINANCIAL MARKETS

III.2.1 Interest rates

Chart III.7
THE CNB RAISED KEY INTEREST RATES
(percentages)

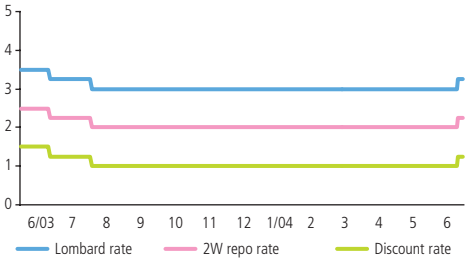


Chart III.8
MARKET INTEREST RATES MOSTLY ROSE
(percentages)

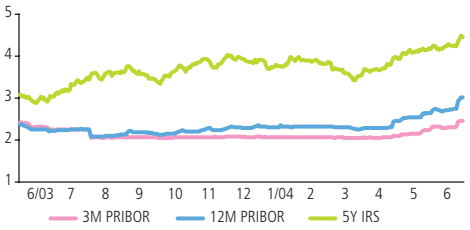
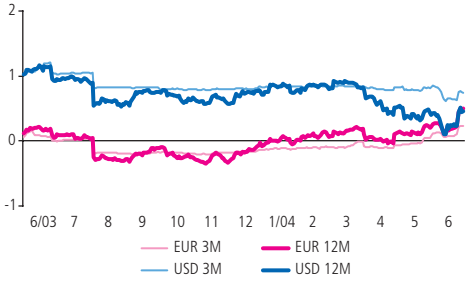


Chart III.9
THE INTEREST RATE DIFFERENTIALS VIS-À-VIS THE EURO AND DOLLAR SHOWED MIXED DEVELOPMENTS
(percentage points)



Interest rates mostly rose in 2004 Q2. The growth was closely connected with the publication of the CNB's new macroeconomic forecast, which implied a gradual rise in interest rates sooner than most market participants had expected. Other domestic and foreign factors were less significant as regards their effect on rates. Nevertheless, they affected the rate level at least in the short term. Following the publication of the lower-than-expected inflation in May (after the Czech Republic's entry into the EU) the rise in rates temporarily halted. The worsened international political situation after the terrorist attacks in Iraq and Saudi Arabia also led to a temporary levelling off of interest rates. Sentiment on the developed markets regarding expectations of an early increase in key interest rates acted in the opposite direction. At the end of June, the CNB increased its key interest rates by 0.25 percentage point. The 2W repo rate was increased to 2.25%, the Lombard rate to 3.25% and the discount rate to 1.25% with effect from 25 June 2004. Market rates responded with a further rise at all maturities. This was also due to the fall of the coalition government. PRIBOR spot quotations and FRA forward quotations at the end of June indicated a further rise in interest rates going forward.

The PRIBOR yield curve gradually shifted to a higher level, especially at its longer end. Its slope therefore became more positive. The spread between the 1Y PRIBOR and the 2W PRIBOR reached 0.68 percentage point in June. The IRS yield curve also moved to a higher level, the largest changes being visible in the central part of the curve. Nevertheless, the changes were more balanced than in the case of the money market yield curve. The average 5Y-1Y spread in June was 1.45 percentage points and the 10Y-1Y spread 2.11 percentage points.

The interest rate differential (PRIBID/CZK-LIBOR/EUR,USD) was affected by interest rate developments both abroad and on the domestic interbank market. Although key rates remained unchanged in both the most important economies, they were expected to increase and so market interest rates grew. In the euro area the repo rate was 2.0%, while in the USA the O/N rate was 1.0%. Interest rates rose fastest on the money market in the USA, hence the interest rate differential vis-à-vis dollar rates narrowed somewhat, whereas the differential vis-à-vis euro rates increased.

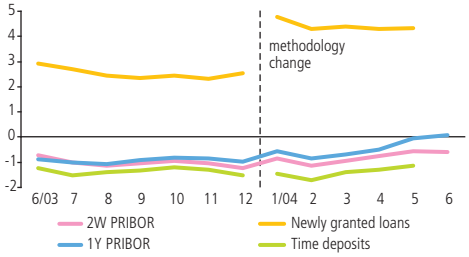
Six auctions were held on the primary government bond market, with original maturities ranging from 5Y to 15Y and a total volume of CZK 29.9 billion. The Ministry of Finance temporarily suspended its programme of reverse auctions, under which it had tried to buy soon-to-mature government bonds in order to support the liquidity of other issues. Its stated reason for doing so was the unfavourable situation on the domestic and foreign bond markets. The Ministry of Finance issued its first-ever 10-year koruna eurobond, which was increased to EUR 1.5 billion thanks to strong interest. The interest rate is 4.625%, i.e. 0.225 percentage point above the yield on the comparable German Bund. The issue was given an A- rating with a stable outlook. The rating is in line with the Czech Republic's long-term foreign currency rating.

On the mortgage market, there were securities issues amounting to CZK 3.3 billion. Issuing activity also continued on the primary koruna eurobond market, where the outstanding volume at the end of June 2004 was CZK 145.6 billion.

Client interest rates[12] also responded partly to interest rate movements on the financial market. Nominal interest rates on new loans went up slightly to 5.4%, whereas rates on new deposits were more or less flat at 1.4%.

Real interest rates[13] were affected not only by the level of nominal rates, but also by how the price indices developed. Expected consumer price indices are higher on a long-term basis than expected industrial producer price indices. This fact is reflected in the levels of the individual real interest rates. Real rates on new loans were 4.3% in May, while real rates on time deposits were -1.1%.

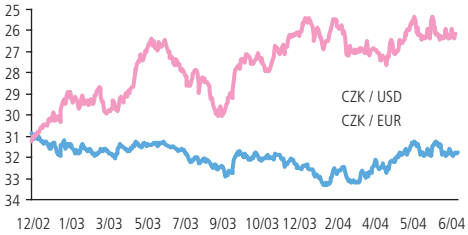
Chart III.10
EX ANTE REAL INTEREST RATES SHOWED MIXED DEVELOPMENTS
(percentages)



III.2.2 The exchange rate

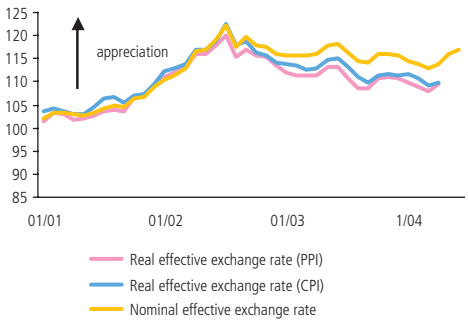
The average exchange rate of the koruna against the euro in 2004 Q2 was CZK 32.0/EUR, which represents a year-on-year depreciation of almost 2%. However, the nominal exchange rate of the koruna tended to appreciate during the quarter. The koruna started appreciating from around CZK 33.0/EUR at the turn of March and April to around CZK 31.3/EUR at the end of June. One of the probable reasons for the change in trend was a change in financial market expectations, due primarily to the publication of information from the April inflation forecast containing a sizeable increase in inflation and monetary policy interest rates. In addition to a halt in short-term capital outflow, the koruna's exchange rate was affected by a change in portfolio investment flows, in particular a year-on-year rise in non-residents' demand for domestic securities and a decline in residents' interest in foreign bonds. In the last third of June, the koruna depreciated slightly (from around CZK 31.3/EUR to approximately CZK 31.7/EUR), owing to events on the domestic political scene.

Chart III.11
THE KORUNA'S EXCHANGE RATE AGAINST THE EURO APPRECIATED IN 2004 Q2



The koruna's exchange rate against the dollar was CZK 26.6/USD on average in 2004 Q2, a year-on-year appreciation of approximately 4%. However, the koruna's year-on-year rate of appreciation slackened markedly by comparison with Q1 and with the previous two years. Given the relative stability of the dollar against the euro, the koruna-dollar exchange rate was affected during the quarter chiefly by the koruna's general appreciation tendency. The koruna's exchange rate against the dollar appreciated from around CZK 27.0/USD at the beginning of the quarter to around CZK 25.5/USD at the end of the second third of June. Owing to the aforementioned uncertain situation on the domestic political scene, the koruna depreciated slightly at the close of June, but this depreciation was rather stronger than against the euro (to CZK 26.5/USD) owing to the evolution of the dollar on world markets.

Chart III.12
THE NOMINAL EFFECTIVE EXCHANGE RATE APPRECIATED IN Q2
(Year 2000 = 100)



The nominal effective exchange rate of the koruna appreciated slightly year on year in 2004 Q2 (by approximately 1.5%). This chiefly reflected the koruna's appreciation against the dollar. In January to May, the year-on-year depreciation of the koruna's real effective exchange rate continued amid deflation of both the CPI and the PPI. This tendency primarily reflected the lower inflation in the Czech Republic than abroad.

12 Client interest rates underwent a change in methodology at the beginning of 2004. Newly drawn credits were replaced by newly extended loans, the deciding date for which is the date of conclusion of the loan agreement. This better reflects the demand for loans at any given interest rate. This approach is in line with ECB methodology.

13 Ex ante real interest rates: nominal interest rates on loans are deflated by the industrial producer price indices expected by the CNB each month; nominal interest rates on deposits and PRIBOR rates are deflated by the consumer price indices expected by financial market participants each month.

III.2.3 Capital flows

The financial account recorded a surplus of only CZK 3.6 billion in 2004 Q1, i.e. a decline to approximately one tenth of the 2003 Q1 surplus (CZK 34.5 billion). This considerable year-on-year fall in the net inflow of foreign capital was due mainly to a decrease in short-term liabilities of domestic banks abroad. Other capital flows conversely saw more favourable year-on-year developments. A significant change occurred in the portfolio investment area, where an almost two-year-long capital outflow was replaced by an inflow. The financial account surplus in 2004 Q1 was attributable especially to direct and portfolio foreign investment, as well as to a decrease in domestic entities' foreign bond holdings.

The net inflow of foreign capital in 2004 Q1 amounted to CZK 30.1 billion (compared to CZK 27.2 billion in the same period of 2003). Foreign direct investment totalled CZK 31.5 billion, around 60% of it being reinvested earnings of non-residents and the rest being inflow of capital from abroad. The largest share of the inflow of capital from abroad was investment in manufacturing (around 50%), investment in real estate (around 25%) and the building of wholesale and retail networks (around 20%). From the geographical point of view, the biggest direct investors remained the Netherlands and Netherlands Antilles and Japan. Significant inflows of capital also came from Canada, Germany and Slovakia. Czech direct investment abroad remained negligible (CZK 1.4 billion), despite rising year on year.

The net inflow of portfolio investment in Q1 was CZK 25.6 billion. In the same period a year earlier there had been an outflow of capital of CZK 32.7 billion. The considerable year-on-year change in portfolio investment flows was mostly due to a decline in residents' interest in foreign debt securities (by almost CZK 50 billion year on year). A roughly two-year-long outflow of capital resulting from residents' interest in foreign bonds changed into an inflow at the beginning of 2004 due to a decline in holdings (of CZK 11.7 billion). Several factors seem to have led to this change, ranging from expected growth in interest rates abroad, the lacklustre results of domestic investment funds through to a preference for domestic investments. At the same time, non-residents' interest in domestic portfolio investment, in particular shares, approximately tripled year on year. This higher interest was probably caused by the expected greater credibility of the Czech capital market in connection with EU entry and by the improving economic results of domestic firms, enabling growth in dividends. The capital outflow under portfolio investment was thus due solely to residents' growing interest in foreign shares, probably reflecting the onset of economic recovery in EU countries.

Other investment recorded a net outflow of CZK 51.8 billion in 2004 Q1. This was mainly due to the banking sector, primarily through a decline in short-term liabilities. A moderate outflow of capital via short-term loans extended was also recorded in the business sector.

In 2004 Q2, international reserves were affected by the CNB Bank Board's April decision to sell off income on these reserves through the foreign exchange market (CZK 5.2 billion for 2004 Q2). The change in the reserves in Q2 was thus due almost solely to valuation changes. In koruna terms the value of the reserves fell from CZK 724.9 billion to CZK 691.9 billion in the course of Q2, owing to the koruna's appreciation against the euro and the dollar. The dollar value of the reserves fell from USD 27.0 billion to USD 26.5 billion during Q2.

Table III.3
THE FINANCIAL ACCOUNT SURPLUS FELL SHARPLY YEAR ON YEAR IN Q1
(CZK billions)

	2001 Q1	2002 Q1	2003 Q1	2004 Q1
Financial account	36.9	54.3	34.5	3.6
Direct investment	46.7	27.8	27.2	30.1
- Czech abroad	-1.4	-0.7	0.0	-1.4
- Foreign in Czech Republic	48.1	28.5	27.2	31.5
Portfolio investment	9.5	7.8	-32.7	25.6
- Czech abroad	-1.9	-13.7	-39.9	3.6
- Foreign in Czech Republic	11.4	21.5	7.2	22.0
Financial derivatives	0.3	-0.1	-0.6	-0.3
Other investment	-19.6	18.8	40.6	-51.8
1. Long-term investment	-4.2	13.6	23.7	4.5
- Credit granted abroad	-6.6	14.8	14.8	2.5
- Credit accepted from abroad	2.4	-1.2	8.9	2.0
2. Short-term investment	-15.4	5.0	16.9	-56.3

Chart III.13
FOUR COUNTRIES DOMINATED THE GEOGRAPHICAL STRUCTURE OF FDI IN 2004 Q1

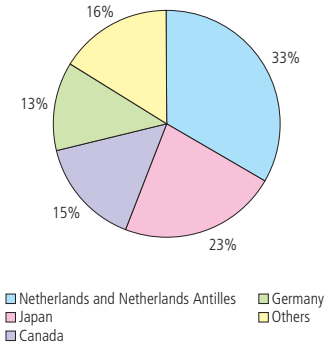


Chart III.14
THE NET OUTFLOW OF PORTFOLIO INVESTMENT GRADUALLY CHANGED INTO A NET INFLOW

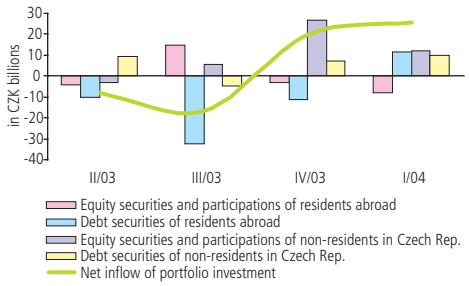
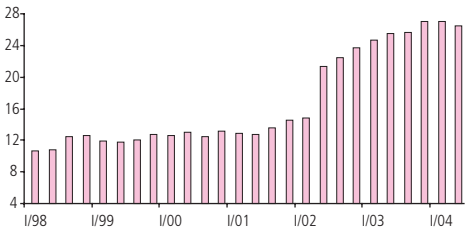


Chart III.15
THE INTERNATIONAL RESERVES DECREASED IN DOLLAR TERMS IN 2004 Q2
(USD billions)



III.3 DEMAND AND OUTPUT

According to the CZSO's latest estimate, economic growth in the Czech Republic slowed modestly in 2004 Q1, to 3.1%.[14] Compared to the previous quarter the growth was 0.2 percentage point lower. The economy grew for the sixth consecutive year, but the output gap remained negative.[15]

The continuing economic growth was still underpinned by rising domestic demand. Developments on the demand side, however, confirmed a significant change compared to the previous period – until 2003 Q3 the growth of the Czech economy had been connected above all with a steady rise in household consumption, whereas in 2003 Q4 rapidly rising investment demand took over as the main driver of GDP growth. The strengthening investment demand was mainly due to improving export results, the external demand outlook and the easy monetary conditions (especially the exchange rate component thereof). However, the contribution of household consumption to GDP growth was still significant. On the other hand, the growth was no longer supported by final consumption of general government, which declined in Q1.

The external sector again did not contribute to the GDP growth in 2004 Q1, and its negative contribution increased further. The continuing external demand recovery, the koruna's easy exchange rate and continuing structural changes in the corporate sector fostered a further pick-up in goods export growth. Imports of goods, however, again grew even faster. The acceleration of import growth was connected with a more pronounced strengthening of domestic investment demand growth, satisfied to a large extent by imports.

The continuing external demand recovery in the countries which are the Czech Republic's major trading partners was confirmed by the latest estimates of economic growth in EU countries/the euro area and some transition economies. The economic growth in EU countries was still heavily supported by rising government expenditure, but a more significant factor from the point of view of Czech exports was a sharp increase in foreign trade activity (especially imports). Also important was a recovery in investment demand, suggesting a positive economic outlook. GDP growth was also quite fast in Slovakia and some other transition economies.

III.3.1 Domestic demand

Domestic demand remained the main engine of economic growth in 2004 Q1. Final domestic demand growth eased, but remained fairly buoyant (4.2% year on year). The slower growth was due primarily to declining government final consumption expenditure, which had been recording annual growth until the end of 2003. Growth in household consumption expenditure was roughly flat at the level of the previous quarter. Thus, the surge in investment demand did not fully compensate for the impact of the falling government expenditure on domestic demand. However, aggregate domestic demand growth picked up pace in 2004 Q1 (to 5.3%), owing to larger additions to inventories.

CHART III.16
ECONOMIC GROWTH SLOWED SOMEWHAT, BUT REMAINED ABOVE 3%
(annual percentage changes)

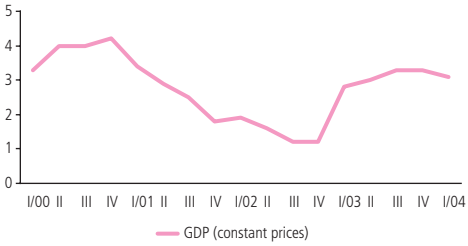


CHART III.17
THE GDP GROWTH IN 2004 Q1 WAS SUPPORTED BY DOMESTIC DEMAND
(annual percentage changes in CZK billions; constant prices)

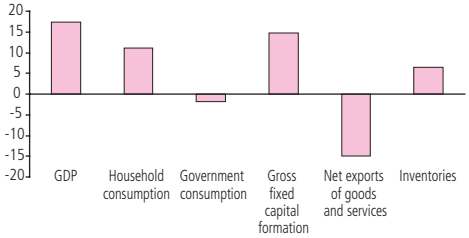


TABLE III.4
THE CONTINUING ECONOMIC GROWTH RECOVERY IN EU COUNTRIES FOSTERED BETTER CONDITIONS FOR CZECH EXPORTS
(annual percentage changes; seasonally adjusted; source: Eurostat)

	Euro area		EU-15	
	2003 Q4	2004 Q1	2003 Q4	2004 Q1
Gross domestic product	0.7	1.3	1.0	1.6
Final consumption expenditure of households and non-profit institutions	0.7	0.9	1.0	1.3
Government final consumption expenditure	2.2	1.5	2.5	2.0
Gross fixed capital formation	0.0	1.0	0.5	1.7
Domestic demand	1.2	1.1	1.4	1.5
Exports of goods and services	0.3	3.4	1.1	2.9
Imports of goods and services	1.7	2.9	2.1	2.5

TABLE III.5
THE ANNUAL GROWTH IN DOMESTIC DEMAND AND GDP IN 2004 Q1 WAS SUPPORTED BY INVESTMENT AND CONSUMER DEMAND
(percentages, CZK billions)

	2003 Q1	2003 Q2	2003 Q3	2003 Q4	2003	2004 Q1
Gross domestic product	2.8	3.0	3.3	3.3	3.1	3.1
Aggregate demand (domestic demand and exports)	4.1	4.9	5.5	5.8	5.1	6.5
Total domestic demand a)	3.9	5.2	4.1	4.9	4.5	5.3
Final domestic demand b)	4.9	5.2	5.2	4.7	5.0	4.2
of which:						
Household consumption	5.1	5.2	5.6	3.8	4.9	3.9
Government consumption	2.9	3.7	0.2	2.0	2.2	-1.6
Non-profit institutions serving households	5.5	3.2	2.5	1.6	3.2	4.9
Gross fixed capital formation	6.2	6.3	8.3	8.5	7.4	9.5
Imports of goods and services	5.6	7.4	8.7	9.6	7.9	11.3
Exports of goods and services	4.5	4.4	7.8	7.0	5.9	8.3
Net exports of goods and services (balance. CZK billions)	-24.3	-39.6	-48.2	-71.8	-183.8	-39.1

a) including changes in inventories; b) excluding changes in inventories

14 The GDP assessment is based on newly adjusted time series of the GDP component indicators. This revision respects the methodical principles of the European system of accounts (ESA 1995). The CZSO has harmonised the methodology for transposing indicators from current to constant prices. In contrast to the former conversion of the time series into base year prices (previously 1995), the Eurostat methodology is now applied, under which the indicators are converted to average prices of the previous year and then their chaining is done. This procedure more faithfully reflects the changes in the structure of individual components. So far, the new methodology does not provide structural data on GDP developments on the supply side and in the investment area. Therefore, partial indicators were used when assessing these developments.

15 The "output gap" – for details see the box: *Use of the output gap indicator at the CNB* in the October 2003 Inflation Report.

Chart III.18
ANNUAL HOUSEHOLD CONSUMPTION GROWTH WAS VIRTUALLY UNCHANGED FROM THE PREVIOUS QUARTER
(percentages)

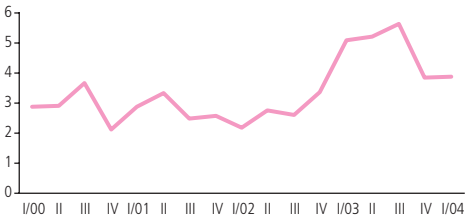


Chart III.19
FASTER GROWTH IN CONSUMPTION EXPENDITURE THAN GROSS DISPOSABLE INCOME FOSTERED A YEAR-ON-YEAR DECREASE IN THE GROSS SAVINGS RATE OF HOUSEHOLDS
(percentages)

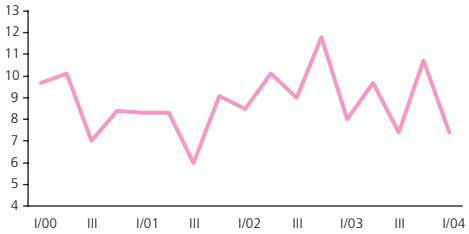
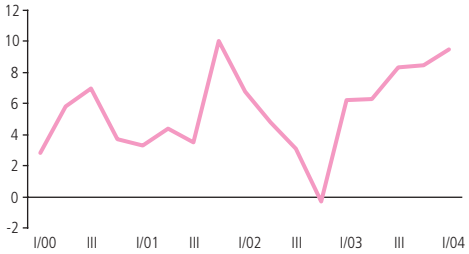


Chart III.20
THE UPWARD TREND IN INVESTMENT GROWTH CONTINUED INTO 2004 Q1
(annual percentage changes)



Consumer demand

Final consumption expenditure of households grew at almost the same pace in 2004 Q1 as in the previous quarter. With a year-on-year increase of 3.9%, its contribution to GDP growth was lower than that of investment demand.

The main source of financing for the still buoyant growth in households' consumption expenditure was their rising income. Above all, there was a significant increase in the growth rate of income from wages, the main component of household income. Wages accounted for around one half of the rise in current income. The faster growth of households' current income than in the previous quarter was also aided by property income and other current transfers. By contrast, income from social benefits showed a continuing downward annual growth trend. The overall annual increase in households' gross disposable income was higher in 2004 Q1 than in the previous quarter (4.7% year on year). Owing to the higher inflation at the beginning of 2004, real growth in gross disposable income was lower than nominal growth, reaching 3.4%.

As in 2003, the increase in gross disposable income did not fully cover the rise in households' consumption expenditure. Therefore, the proportion of households' disposable income saved was again lower in 2004 Q1. Consequently, the volume of gross savings declined annually by 3%. Households also took out loans, although the growth in borrowing was roughly unchanged compared to the same period a year earlier.

The stabilisation of household consumption growth at a considerably lower level than in the first three quarters of 2003 indicated an unwinding of the extraordinary factors influencing households' consumption behaviour (low inflation etc. – for details see the January 2004 Inflation Report). It is probable that households' propensity to consume was also affected by their less optimistic view of past and future economic developments and their living standards, as indicated by consumer confidence surveys (Ecoma plus).

Investment demand

The renewed growth of investment activity in the economy, apparent throughout 2003, continued into the first three months of 2004. The annual growth rate of gross fixed capital increased, reaching 9.5% in Q1. Since revised data on structural developments in investment are not available at present, the evaluation of trends in this area is based primarily on partial indicators. These showed certain structural changes in investment activity in Q1.

General government investment made a major contribution to the growth of overall gross fixed capital formation in 2003 Q4. The sharp annual decline in state budget capital expenditure in Q1 suggests, however, that government investment did not provide much support for overall investment growth. On the other hand, very fast annual investment growth in monitored large companies[16] (by around 8%) suggested that there was an investment growth recovery in the sector of non-financial organisations and corporations, which account for roughly two-thirds of total investment. This recovery reflected improving foreign trade results and prospects, good financial results and low real interest rates on loans. Faster growth of construction investment than investment in machinery also suggested that the pick-up in investment by non-financial corporations was also partly due

16 The contribution of these companies to total book value added was around 70%.

to investors' attempts to realise their intended investments before the VAT increase from 5% to 19% on 1 May 2004 (with the exception of housing construction).

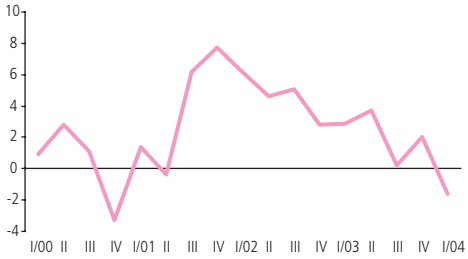
At the beginning of 2004, investment by households seemed to be growing quite quickly as well, as there was a sizeable increase in housing starts and completions. It cannot be ruled out that expectations of changes in VAT on housing construction work (in 2007) also played a role, together with relatively low nominal mortgage rates, uncertainties surrounding rent deregulation and the effects of the Czech Republic's accession to the EU on property prices.

Government demand

Government final consumption expenditure at constant prices fell by 1.6% year on year in 2004 Q1, contrary to the modest increase recorded in the previous year. At current prices, however, government demand maintained its high rate of growth (6.1%), primarily as a result of a sharp increase in general government wage expenditure.

Underlying the government consumption growth in 2004 Q1 were contrary movements in the individual expenditure items of the state budget. Besides wages, the increase in government final consumption expenditure was due to higher non-investment transfers to subsidised organisations and state funds, and other current expenditure. Government debt service expenditure also increased (by 24.5%), owing to interest payments under the repayment schedule for medium- and long-term government bonds in Q1. By contrast, non-investment transfers to municipal and regional budgets recorded a sharp annual decline (of around 22.2%, i.e. almost CZK 9.5 billion). This decline seems to reflect a stabilisation of the situation after the previous year's extraordinary expenses related to the completion of the local government reforms.

Chart III.21
THE STEADY SLOWDOWN IN GOVERNMENT CONSUMPTION GROWTH SWITCHED TO A YEAR-ON-YEAR DECLINE IN 2004 Q1
(percentages)



III.3.2 Net external demand

Although the continuing gradual recovery of economic growth abroad indicated better conditions for Czech exports, net exports of goods and services[17] developed unfavourably in 2004 Q1, as in the previous quarter. Annual export growth picked up pace (to 8.3%), but the growth rate for imports was even higher (11.3%). The lead of import growth over export growth thus slightly increased. Under these circumstances, the tendency of the negative balance of net exports to deepen – present for eight consecutive quarters – continued. In 2004 Q1 alone, negative net exports grew by CZK 14.8 billion year on year, to CZK -39.1 billion. The contribution of net exports to GDP growth thus remained negative.

The causes of the deepening negative balance of net exports remain broadly unchanged. As in the previous quarter, the year-on-year deterioration in net exports was mainly due to a widening of the trade deficit (by CZK 13 billion), since the services deficit widened only slightly (by CZK 1.8 billion). The persisting negative development of the balance of trade primarily reflected faster domestic demand growth and a related increase in imports of goods. The koruna's exchange rate recorded a modest annual depreciation for the third consecutive quarter[18], but this had no significant effect on imports. The continuing relatively fast growth of imports, especially for investment, tended to confirm the increasing import propensity of domestic demand, associated with structural changes on the supply side (due chiefly to competition and specialisation).

Chart III.22
WITH IMPORTS RISING FASTER THAN EXPORTS, NEGATIVE NET EXPORTS INCREASED FURTHER
(annual percentage changes; constant prices)

17 At 2000 prices.

18 In 2004 Q1, the weighted exchange rate of the koruna (EUR, USD) showed a year-on-year depreciation of 0.9%, owing to the weakening of the koruna-euro rate (by 3.9%). By contrast, the koruna-dollar rate appreciated by 10.8% year on year.

Chart III.23
EXPORTS TO ADVANCED MARKET ECONOMIES INCLUDING GERMANY ACCOUNTED FOR THE BULK OF TOTAL EXPORTS
(percentages; current prices; 2004 Q1)

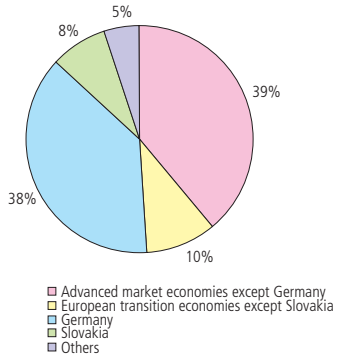


Chart III.24
THE UPTURN IN INDUSTRIAL OUTPUT GROWTH WAS ACCOMPANIED BY FAST EXPORT GROWTH
(percentages; constant prices)

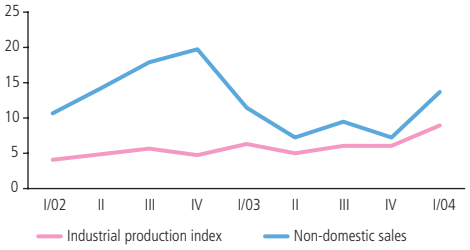
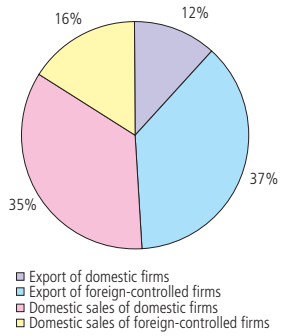


Chart III.25
IN Q1, EXPORTS OF INDUSTRIAL PRODUCTION WERE AGAIN CHIEFLY DUE TO FOREIGN-OWNED COMPANIES
(shares in total industrial sales - domestic and external - at constant prices; 2004 Q1)



Goods exports themselves also grew quite quickly (by 8.2%), although their growth rate was lower than that of goods imports (11.2%). Given that most Czech exports go to EU countries, the favourable evolution of goods exports was supported by the continuing modest depreciation of the koruna-euro exchange rate. At the same time, the positive impact of the continuing economic recovery in the Czech Republic's major trading partner nations started to be felt. The continuing goods export growth was also supported by exports being made to a large extent by foreign-owned companies, whose sales are better secured thanks to extensive distribution networks abroad. Exports to advanced market economies continued to dominate total goods exports, recording a growth rate of over 10% in Q1 (11.5%).[19] Exports to European transition economies increased even faster (by 18.4%). Very rapid growth was also recorded for exports to the Czech Republic's main trading partners – Germany and Slovakia. As for the commodity structure, exports of mechanical and electrical engineering commodities dominated, with a share of 58%.

III.3.3 Gross domestic product

On the supply side of the economy, the growth in gross value added was still mixed across the different branches. The structure of production and book value added[20] indicated that services, industry and construction all contributed to the 3.1% GDP growth in 2004 Q1.

The majority of services branches contributed to the relatively sharp rise in book value added in this sector during the first three months of 2004. The rise was particularly steep in wholesale and retail trade, transport and public services[21], but more moderate in financial intermediation and commercial services. By contrast, book value added growth in communications was flat at the previous quarter's level.

In 2004 Q1, the growth in book value added in industry was more sluggish than that in services, but still reached quite high figures (11.7% year on year). As in previous years, its growth was very mixed across the various industries, as is also apparent from the industrial production index (IPI) during Q1. The acceleration of industrial production growth together with structural changes in the output of individual industries primarily reflected the ongoing changes in domestic and foreign demand. The accelerated IPI growth was aided above all by rising demand for steel and iron on world markets, a demand recovery in electrical engineering, the generally more favourable external demand and the opening of new production facilities by foreign investors (especially for vehicle component production). Growth in construction output, which supported the production of building materials, was also important. Most of these factors contributed to a marked increase in real exports. In 2004 Q1, real export sales in industry rose almost by 14%, accounting for roughly one-half of total sales in industry. As in the previous quarter, about 70% of exports were made by foreign-owned companies.

Value added growth seemed to continue in construction as well, as another strong increase in construction output was recorded, accompanied by buoyant growth in productivity and book value added in large companies (of 18% year on year).

The continuing recovery in industrial production and construction work at the beginning of 2004, together with the rationalisation of production activities (decreasing employment

19 At current prices.

20 The assessment of gross value added is based on financial indicators for companies with 100 employees or more (hereinafter "large companies") for the reasons mentioned in the introduction to this section (see footnote 14).

21 The strong growth in value added in public services was primarily due to increased personnel costs (a significant rise in the average wage).

etc.), created suitable conditions for productivity growth and cost cutting, and consequently for improved financial results in the business sector.

III.3.4 Performance of non-financial organisations and corporations[22]

The trend of improving financial performance in large companies in the sector of non-financial organisations and corporations, apparent since 2003 Q2, continued into 2004 Q1. Corporations' output including business margins increased faster than total costs by comparison with 2003 Q1. The result was a large annual increase in net operating surplus and pre-tax profit (of 27% and 18.7% respectively) and fairly fast growth in net value added per employee.

As in 2003, these favourable results were achieved amid improved profitability indicators – most notably the profit-expenses and profit-equity ratios. The decline in the personnel cost-output ratio also continued, thanks to continuing employment rationalisation in the business sector in conditions of strong competition and coincident output growth. The material cost-output ratio was also lower in Q1 than in the same period a year earlier. Larger increases in prices of metals and some other commodities on world markets fed through into costs and prices in industries directly engaged in metal processing, but for the time being they did not have much effect on the overall cost-output ratios for large non-financial corporations in other sectors. The main features of corporate performance at the beginning of 2004 are also illustrated by a decrease in stock turnover time.

The continuing favourable trend for corporations' financial results fostered an increase in the share of profit-making corporations in the total number of non-financial corporations compared to a year earlier. Conversely, the percentage of corporations that owe wages and corporations with negative equity decreased. As regards ownership structure, foreign-controlled corporations made a major contribution to the buoyant profit growth (28% year on year). Profits of domestic private corporations also grew in Q1 (by 10.5%). Only in the case of domestic public corporations were profits lower.

The main financial performance indicators for large non-financial corporations in Q1 suggested continuing improvement of the corporate sector's financial condition amid recovering external demand and lasting strong competition.

TABLE III.6
GROSS PROFITS RECORDED A LARGE YEAR-ON-YEAR INCREASE IN 2004 Q1
(percentages)

	2004 Q1	
	ORGANISATIONS, TOTAL	INDUSTRY
Income. total	8.1	8.4
Output. total	10.9	10.1
Expenses. total	7.4	7.9
of which: cost of sales	10.4	9.6
personnel costs a)	7.2	6.2
depreciation	3.3	4.9
Book value added	12.1	11.7
Pre-tax profit	18.7	14.5
Net operating surplus	27.0	21.7

a) Comprises wage and other personnel costs, remunerations to members of companies and co-operatives, social security costs and social costs

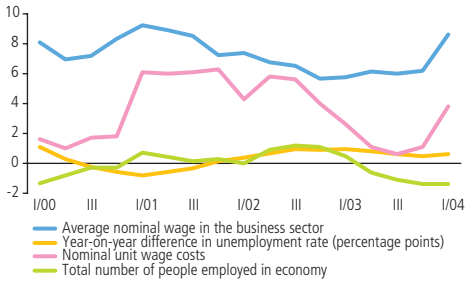
TABLE III.7
THE PERSONNEL COST-OUTPUT RATIO SHOWED A YEAR-ON-YEAR DECLINE AGAIN IN 2004 Q1
(percentages; percentage points; CZK thousands)

	2004 Q1		Change in perc. points against 2003 Q1	
	Organisations, total	Industry	Organisations, total	Industry
Profit-expenses ratio	6.67	8.80	0.63	0.51
Profit-equity ratio	3.47	4.59	0.42	0.29
Profit-sales ratio	6.80	8.85	0.47	0.34
Material cost-output ratio	68.28	71.74	-0.33	-0.39
Personnel cost-output ratio	14.75	11.32	-0.51	-0.42
Ratio of wage costs to value added	33.28	28.63	-1.60	-1.44
	CZK thousands per month		annual percentage changes	
Book value added per employee	51.69	59.81	13.48	14.58

III.4 THE LABOUR MARKET

The developments on the labour market did not suggest any improvement in the relationship between the demand for, and supply of, labour in 2004 Q1. Employment and unemployment in the economy remained under the influence of a number of factors connected above all with the continuing economic restructuring process and the still strong competition. Companies continued to rationalise their production activities, which led to lower costs and higher competitiveness on domestic and foreign markets. As a result of these processes, employment continued to fall and unemployment kept on rising. However, some indicators of the negative tendencies on the labour market became more moderate at the end of 2004 Q2. Unemployment was still partly structural, as evidenced by concurrent modest annual growth in vacancies and an increasing number of people unemployed. Average wage growth in the business sector picked up pace, but labour

CHART III.26
THE DECLINE IN EMPLOYMENT DID NOT DEEPEN IN 2004 Q1
(annual percentage changes and percentage point changes)



22 Assessment based on figures for non-financial organisations and corporations with 100 employees or more, all branches (hereinafter "large companies").

productivity in both industry and construction continued to rise faster than average real wages, and nominal unit wage costs were falling. At the macroeconomic level, however, the growth rate of nominal unit wage costs increased.

III.4.1 Employment and unemployment

The decline in employment did not deepen in 2004 Q1, remaining at the level of 2003 Q4 (-1.4% year on year; LFS). The halt in the decline in employment in the economy occurred amid a concurrent slower decrease in the number of employed persons in the employees category (to 1.6%) and an opposite movement in employment among entrepreneurs.[23] The greater decrease in the number of entrepreneurs was primarily due to amendments to the tax legislation effective from the beginning of 2004.[24] This fact fostered a fall in employment in the tertiary sector at the beginning of 2004. However, the most significant factors influencing employment and unemployment at the beginning of 2004 were continuing restructuring and rationalisation amid strong competition (labour cost reductions etc.), and shifts in demand. To a large extent the unemployment in the Czech economy was also structural in nature, showing up as skills, regional and sectoral gaps between supply and demand. High labour taxation (including social security, health insurance and pension scheme contributions) and the minimum wage also probably fostered higher unemployment.

Although employment went down in all major sectors of the economy, this phenomenon was not entirely across the board in nature. This conclusion was confirmed by mixed employment developments across different branches (services included) in Q1. Increasing employment in a number of branches suggested a link with the structural changes in demand.

Chart III.27
THE GAP BETWEEN LABOUR DEMAND AND SUPPLY NARROWED AT THE END OF 2004 Q2
(seasonally adjusted numbers in thousands)

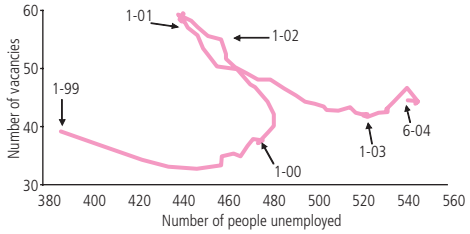


Table III.8
THE CZECH REPUBLIC HAS RELATIVELY HIGH LONG-TERM UNEMPLOYMENT BY INTERNATIONAL COMPARISON
(percentage shares of long-term unemployment in total unemployment; source: CZSO, Eurostat)

	2000	2001	2002	2003
EU (25 countries)	45.5	44.7	44.3	44.0
EU (15 countries)	44.9	41.9	40.3	41.3
Czech Republic	48.3	51.3	50.7	48.7
Slovakia	54.0	58.8	65.2	64.9
Hungary	47.6	44.6	42.9	41.4
Poland	46.3	50.3	54.5	55.7
Slovenia	62.1	60.3	55.7	52.3
Cyprus	25.0	20.5	20.5	25.0
Malta	65.7	47.8	42.7	40.2
Estonia	45.6	48.3	52.6	45.5
Latvia	48.4	56.5	53.7	48.0
Lithuania	57.7	55.8	45.2	41.0

The existence of structural unemployment in the Czech economy was evidenced in particular by rising unemployment on the one hand, and by modest growth in vacancies on the other. The influence of structural factors was also visible in long-term unemployment, which has been rising for two years. As shown in Table III.8, this problem is not specific to the Czech economy. In the Czech Republic, those unemployed for more than one year account for almost 50% of the total unemployed. By comparison with the ten new EU member states, the Czech Republic is among those with a higher share of long-term unemployment in total unemployment.

However, by the end of Q2 certain indicators were suggesting that the gap between the supply of, and demand for, labour was narrowing. In particular, the annual growth in the unemployment rate slowed in comparison with Q1. The number of unemployed persons per vacancy also recorded a year-on-year decrease in June.

III.4.2 Wages and productivity

Growth in the average nominal wage in the monitored organisations increased rapidly in 2004 Q1 (to 8.8% year on year), exceeding the growth rate of the past two years. A pick-up in average nominal wage growth occurred in the business sector, while in the non-business sector annual wage growth was flat at the level of 2003 Q4.

23 i.e. entrepreneurs with employees, entrepreneurs without employees, and co-operating family members.

24 The change from the previous annual growth to a modest decline was probably linked with the introduction of a higher assessment base for social security and health insurance and the introduction of a minimum tax on entrepreneurs.

The higher increase in wages in the business sector was due to several factors. In particular, it reflected the mostly favourable financial results of corporations in 2004 Q1, which allowed bonuses to be paid. The growth in wages was also partly fostered by an increase in the minimum wage and stricter conditions for the payment of sickness benefits from January 2004, as these measures led to the dismissal of employees and a decrease in the sickness rate among employees with low incomes. These factors probably contributed to the extraordinary wage growth in the business sector, which exceeded 8%. The pick-up in average wage growth was also supported by an increase of one in the number of working days and by the fact that 2004 is a leap year. In the non-business sector, the growth rate of average nominal wages was unchanged at the beginning of 2004 – as in the previous quarter wages rose by 9.7%. The higher wage growth rate in this sector was due to a January 2004 pay review.[25]

Given the higher rate of inflation, however, average real wage growth in Q1 was not substantially different from the figures recorded in the last two years. At 6.4%, it increased only modestly compared to the previous quarter. The most important factor as regards inflation, though, was how wages developed in relation to productivity indicators.

Given the lower GDP growth, whole-economy labour productivity growth slowed in 2004 Q1. Total employment in the economy also dropped, but this was not sufficient to offset the negative influence of the lower GDP growth on whole-economy labour productivity. At the same time, growth in the volume of wages and salaries in the economy picked up, owing to the stronger increase in average nominal wages. The lower growth in whole-economy labour productivity together with the larger increase in the volume of wages and salaries in the economy meant that nominal unit wage costs at the macroeconomic level rose faster in 2004 Q1 than in the previous quarter (3.8%; see Table III.9). In industry and construction, however, the rapid productivity growth continued (by more than 10% and 15% respectively)[26], exceeding the growth rate of average real wages. As a result, nominal unit wage costs in both industry and construction recorded year-on-year declines and there were no upward wage-cost pressures on prices in these sectors. Wage growth in the non-business sector can thus be regarded as the primary cause of the faster nominal unit wage cost growth at the macroeconomic level.

III.5 OTHER COSTS AND PRODUCER PRICES

Other costs continued to show mixed developments in 2004 Q2, but on the whole they indicated stronger inflationary cost pressures compared to the beginning of 2004. Import prices in the majority of import categories were showing annual growth. The continuing upswing in prices of imported inputs fed through – with a lag – into industrial producer prices. However, their stronger influence was apparent only in industries directly engaged in processing imported inputs (above all oil and metals) whose prices rose rapidly on world markets. Producer prices in the food industry also recorded faster growth, owing to persisting strong growth in agricultural producer prices. Although overall growth in industrial producer prices increased markedly in 2004 Q2, modest growth or even a decline in prices continued in the vast majority of manufacturing industries. Inflation was also subdued in market services for the business sector. But prices of construction work recorded an annual increase at the end of 2004 Q2.

TABLE III.9
AVERAGE NOMINAL WAGE GROWTH ROSE TO A TWO-YEAR HIGH IN 2004 Q1
(annual percentage changes)

	2002	2003 Q1	2003 Q2	2003 Q3	2003 Q4	2003	2004 Q1
Average wage in monitored organisations							
nominal	7.3	7.2	6.8	6.3	6.9	6.8	8.8
real	5.4	7.6	6.7	6.4	6.1	6.7	6.4
Average wage in business sector							
nominal	6.5	5.6	6.0	6.1	6.0	5.9	8.6
real	4.8	6.0	5.9	6.2	5.2	5.8	6.2
Average wage in non-business sector							
nominal	9.8	13.9	9.2	7.5	9.7	10.1	9.7
real	7.9	14.4	9.1	7.6	8.8	10.0	7.2
Whole-economy labour productivity	0.8	2.7	3.7	4.4	4.5	3.8	3.9
Nominal unit wage costs	4.9	2.6	1.1	0.6	1.1	1.4	3.8

CHART III.28
THE SLOWING GDP GROWTH IN 2004 Q1 FOSTERED A REDUCTION IN AGGREGATE PRODUCTIVITY GROWTH
(annual percentage changes)

CHART III.29
OVERALL, NOMINAL UNIT WAGE COSTS ROSE YEAR ON YEAR IN EARLY 2004
(percentages)

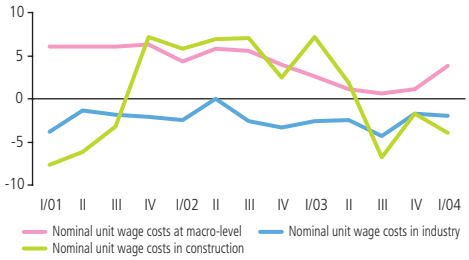
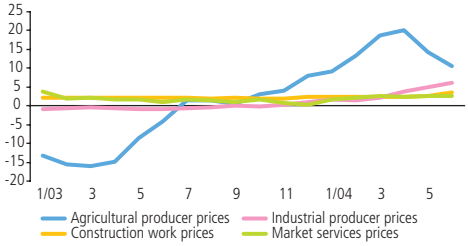


CHART III.30
THE UPSWING IN AGRICULTURAL AND INDUSTRIAL PRODUCER PRICE INFLATION CONTINUED INTO 2004 Q2
(annual percentage changes)



25 A pay adjustment connected with the implementation of broadened wage scales.

26 In industry this refers to sales productivity at constant prices. In construction it means productivity per employee from the "S" value (construction work according to supplier contracts) for a set of corporations with 20 employees or more.

Chart III.31
THE ANNUAL RISE IN IMPORT PRICES WAS DUE CHIEFLY TO IMPORT PRICES OF MINERAL FUELS, RAW MATERIALS AND SEMI-MANUFACTURES
(percentages, percentage points)

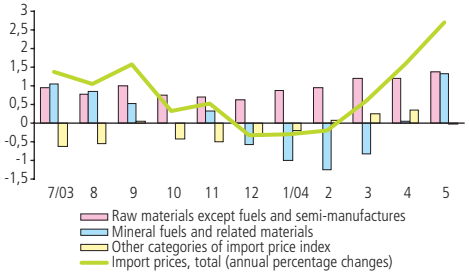


Chart III.32
THE IMPACTS OF WORLD PRICES OF ENERGY-PRODUCING MATERIALS ON IMPORT PRICES CONTINUED TO BE CORRECTED BY THE KORUNA-DOLLAR EXCHANGE RATE
(annual percentage changes)

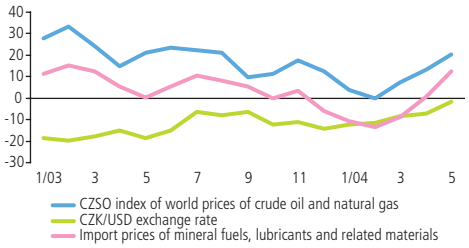
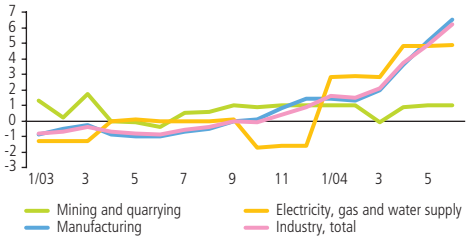


Table III.10
ANNUAL IMPORT PRICE INFLATION INCREASED IN NUMEROUS IMPORT CATEGORIES
(percentages)

	12/03	1/04	2/04	3/04	4/04	5/04
Imports. total	-0.3	-0.3	-0.2	0.6	1.6	2.7
Food and live animals	2.6	1.2	3.8	2.9	3.9	5.0
Beverages and tobacco	3.5	2.8	3.6	4.7	4.4	7.9
Crude materials except fuels	3.9	4.2	5.5	7.7	7.9	13.4
Mineral fuels and related products	-6.1	-10.7	-13.5	-8.6	0.5	12.5
Animal and vegetable oils	-2.7	-2.0	-0.4	2.8	2.6	3.9
Chemicals and related products	0.2	1.0	1.9	2.0	1.8	1.0
Manufactured goods classified by material	2.4	3.5	3.7	4.4	4.4	4.3
Machinery and transport equipment	-1.2	-0.6	-0.4	-0.1	-0.2	-0.2
Miscellaneous manufactured articles	-1.0	-0.5	-0.1	0.2	-0.4	-0.7

Chart III.33
THE UPWARD TREND IN ANNUAL INDUSTRIAL PRODUCER PRICE INFLATION CONTINUED INTO 2004 Q2
(percentages)



III.5.1 Import prices

Given the high openness and import propensity of the Czech economy, import prices are an important inflation factor. The upswing in import prices at the end of 2004 Q1 after three months of decline was primarily due to prices of raw materials and food on world markets. According to the latest figures for May, the annual growth in import prices was 2.7%.

The acceleration of annual growth in world prices of food and raw materials from 5.5%[27] in Q1 to 13.9% in June was caused above all by an upturn in oil prices, which are the most important component of the CZSO's index of world prices of food and raw materials.[28] Prices of Brent crude oil rose only modestly in January, and even declined in February, but since March their annual growth has accelerated quite quickly (to 36.4% in Q2). As in Q1, the increase in the CZSO's raw materials index was also largely due to continuing very buoyant growth in metal prices[29], which averaged 34.3% in Q2. Prices of the other monitored raw materials and food also posted stronger growth in Q2 (to 7.3%). On the contrary, prices of natural gas showed a modest annual decline in the same period.

However, the pick-up in world prices of raw materials and food did not pass through fully into import prices, as its impact was corrected by the koruna-dollar exchange rate, which was still appreciating year on year in Q2.[30]The depressive effect of the koruna-dollar rate was particularly apparent for raw materials, where imports are paid for primarily in dollars. By contrast, the modest depreciation of the koruna-euro rate led to stronger growth in some import prices.

The still fairly differential evolution of raw materials prices and the koruna-dollar and koruna-euro exchange rates passed through with different direction and mixed intensity into the individual items of the CZSO's import price index. According to the latest figures for May, however, import items with rising prices now predominated. Prices of non-energy-producing commodities and semi-manufactures, especially metals and iron scrap, were the major contributor to the faster growth in import prices (to 2.7% in May). There was also a significant change in energy-producing raw materials prices, where the previous relatively sharp decline turned to growth in April. Other import prices also contributed to the annual import price growth. Only in the case of imported higher value added products (machinery and transport equipment, miscellaneous manufactured articles) did import prices continue to fall annually.

III.5.2 Producer prices

Industrial producer prices

Industrial producer prices in 2004 Q2 conformed to the expectation that the gradually slackening disinflation in this price segment would culminate in more stable price growth. In Q2, annual industrial producer price inflation accelerated considerably, reaching 6.2% according to the latest figures for June, which is the highest value since March 1998. The

27 i.e. the average for the quarter.

28 The weight of oil in the CZSO's index of world prices of raw materials and food is 37.29%.

29 The weight of metals prices in the index of world prices of raw materials and food is 8.38%.

30 In Q2, the koruna-dollar exchange rate recorded an annual appreciation of 4%, whereas the koruna-euro exchange rate depreciated annually by 1.8%.

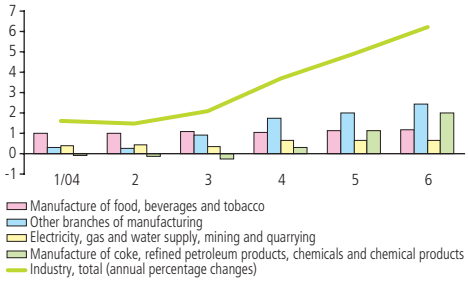
causes of the continuing acceleration in industrial producer price inflation were unchanged: primarily lagged pass-through of the pick-up in import prices and the still fast rise in input prices in the food industry.

All major industrial sectors contributed to the considerable rise in industrial producer prices in 2004 Q2, although prices in manufacturing showed the fastest growth (6.5% in June). The pick-up in producer price inflation was due in large measure to continuing fast growth in metals prices on world markets. Its pronounced effect was visible in basic metals and fabricated metal products, where gradual price growth transformed into a 20% annual increase in June. A large increase was also recorded by prices in the manufacture of coke and refined petroleum products. Due to sharply rising oil prices on world markets and higher coke product prices, the annual price decline in this sector in early 2004 was replaced by a very sharp acceleration in prices in Q2, to 41.4% in June. The price growth in the food industry was not so pronounced in Q2 (from 5% in March to 5.5% in June), but the contribution of food prices to inflation in industry remained significant. Quickly rising prices of inputs remained the driving force of the continuing price rise in this sector (see *Agricultural producer prices*).

In Q2, inflation also accelerated in non-manufacturing industries. Owing to higher demand for coal, prices in mining and quarrying rose after a period of stagnation. Annual inflation also increased in the electricity, gas and water supply industry (to 4.9% in June).

Although industrial producer prices rose quite sharply in 2004 Q2, the price growth in this sector remained very mixed and was not across the board in nature. Especially in higher value added manufacturing sectors, producer prices were broadly flat year on year. The cost-push inflationary pressures resulting from the gradual growth in imported raw material inputs and some intermediate goods were not yet reflected in the prices of these producers.[31]The potential external cost pressures were partly offset by the continuing decline in the personnel cost-output ratio in the corporate sector and, in the case of exporters, by the favourable terms of trade.

Chart III.34
ALL THE MAJOR INDUSTRIAL PRODUCTION CATEGORIES CONTRIBUTED TO THE ANNUAL PICK-UP IN ANNUAL INDUSTRIAL PRODUCER PRICE INFLATION
(percentages, contributions in percentage points)

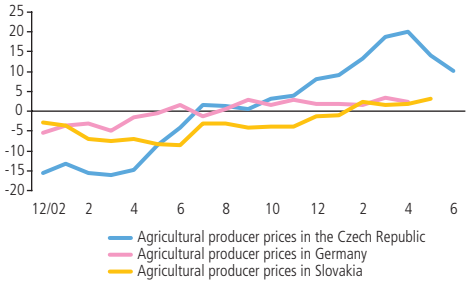


Agricultural producer prices

Agricultural producer prices continued to grow very quickly in 2004 Q2. After accelerating sharply to a historical high in April (20.1%), agricultural producer price inflation fell back slightly in May and June. In June, the annual figure was close to 10%. As in 2003 H2, this still very fast growth was due mainly to crop products, whose annual growth rates reached extraordinary values (17% in June). Most crop commodities recorded buoyant price rises, with cereals and potatoes showing the fastest growth. The continuing rapid increase in crop prices was still due to excess demand on the agricultural commodities market resulting from the adverse weather in the Czech Republic and other European countries in 2003.[32]

Livestock product prices rose much more slowly than crop product prices (by 6.7% in June). The continuing price upswing in this segment was connected mainly with lower domestic and foreign supply of certain commodities. The gap between the demand for, and supply of, livestock products was also widened by new opportunities to export some commodities at higher prices after the Czech Republic's accession to the EU.

Chart III.35
ANNUAL AGRICULTURAL PRODUCER PRICE INFLATION SLOWED, BUT REMAINED QUITE HIGH
(percentages)



31 Out of the 14 manufacturing sectors, only four experienced fast growth in prices (ranging between 5.5% and 41.5% year on year). In eight sectors the growth did not exceed 1.5%, and two sectors saw annual declines in prices.

32 For details see the April 2004 Inflation Report.

Chart III.36
THE FAST ANNUAL GROWTH IN AGRICULTURAL PRODUCER PRICES IN 2004 Q2 WAS DUE MAINLY TO CROP PRODUCTS
(percentages)

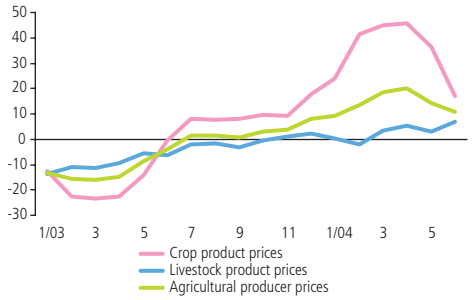
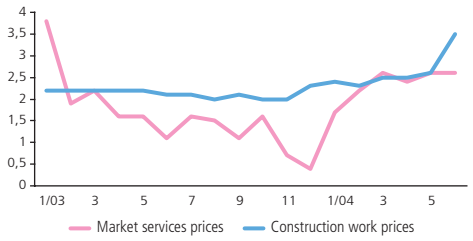


Chart III.37
ANNUAL CONSTRUCTION WORK PRICE INFLATION ACCELERATED AT THE END OF 2004 Q2
(percentages)



Overall, the continuing fast growth in agricultural producer prices exerted upward cost pressures on food industry prices (see *Industrial producer prices*) and consequently on retail food prices. However, an analysis of the "product vertical" suggests that these cost pressures were not fully reflected in production and consumer prices. In a situation where the growth in agricultural producer prices was being driven by only a limited number of crop commodities, some of the cost pressures on prices in manufacturing were "suppressed" for the time being by lower margins.

Other producer prices

The gradual modest strengthening of construction work price inflation ongoing since the end of 2003 switched to sharper annual growth in prices at the end of 2004 Q2 (to 3.5%). This development was probably linked primarily with rising demand for building work, as prices of materials and products consumed in the construction industry also increased in Q2. By contrast, growth in prices of market services for the business sector was flat in Q2 at the end-Q1 level (2.6% year on year). Within market services, the fastest growth was recorded in the categories of sewage collection charges, business services, real estate and rental activities, and financial intermediation. The other components of this index rose only modestly. Overall, market services price inflation remained subdued in 2004 Q2 and did not pose a significant risk to consumer price inflation.

IV. THE MACROECONOMIC FORECAST AND ITS ASSUMPTIONS

IV.1 EXTERNAL ASSUMPTIONS OF THE FORECAST

Assumptions made about the external environment are a crucial condition for the construction of the forecast. For this purpose, the CNB has as usual drawn on the publication Consensus Forecast, which brings together the forecasts of a whole range of foreign analytical teams. According to the latest issue of this publication, the outlook for GDP growth in EU countries is almost unchanged from the last forecast. The same applies to the new member states, where the growth prospects remain favourable.

However, the key factor for the forecast is what happens in Germany, which represents all foreign countries in the CNB's forecasting system. While the expected GDP growth remained virtually the same as in the last forecast (at 1.7%), there was an increase in the expected rates of growth of consumer prices and industrial producer prices. The forecasted consumer price inflation in 2004 is 1.5%, as opposed to 1.2% in the last forecast. Industrial producer prices are expected to grow by 1.1%, compared to the 0.5% estimate from April. The increase in expected inflation clearly reflects the observed pick-up in inflation in 2004 Q1, caused primarily by rising prices of oil and certain other commodities on world markets. In 2005, GDP growth in Germany should reach 1.7% amid slower consumer price inflation of 1.3% and slightly higher producer price inflation of around 1.3%.

During 2004 Q2, the price of Ural crude oil on world markets deviated upwards by 13% from the assumption used in the April forecast. As a result, the Consensus Forecast has shifted upwards across the whole forecast period. The forecast assumes a Ural crude oil price of around USD 31 a barrel in the coming quarter, then a gradual decline to slightly under USD 28 a barrel at the end of 2005.

Table IV.1
EXTERNAL ASSUMPTIONS OF THE FORECAST

	I/04	II/04	III/04	IV/04	I/05	II/05	III/05	IV/05
Ural crude oil prices (USD/barrel)	29.8	32.2	32.7	30.1	28.8	28.1	28.0	28.0
Natural gas prices (by import structure, USD/1000m^3)	122.6	131.06	140.2	144.9	145.7	144.90	143.6	142.6
GDP in Germany (annual, in per cent)	0.7	1.9	2.0	2.2	2.1	1.5	1.6	1.6
Producer price inflation in Germany (annual, in per cent)	0.1	1.4	1.4	1.5	1.8	1.1	1.1	1.1
Consumer price inflation in Germany (annual, in per cent)	1.1	1.8	1.7	1.8	1.6	1.2	1.3	1.2
Nominal USD/EUR exchange rate	1.249	1.204	1.232	1.225	1.227	1.231	1.230	1.218
1Y EURIBOR	2.1	2.3	2.4	2.5	2.7	2.9	3.0	3.2

IV.2 INTERNAL ASSUMPTIONS OF THE FORECAST

In addition to assumptions regarding the external environment, assumptions regarding the domestic economy are an important input for the forecast. These include above all the expected impact of fiscal policy on the economy. The assessment of the effect of fiscal policy, which is derived from assumptions regarding the evolution of the public budget deficit, excluding net lending and subsidies to transformation institutions, is unchanged from the last forecast. The expected 2004 public budget deficit (using revised GDP data) remains at 4.6% of GDP, and a slight fall to around 4.2% of GDP is expected for 2005. Based on these assumptions, the forecast is for a slightly positive contribution of fiscal policy to GDP growth in 2004 and a neutral effect in 2005.

Assumptions regarding the equilibrium values of key macroeconomic variables also have an important position among the internal factors. These assumptions, together with information about the current situation in the economy, allow us to assess the starting conditions of the forecast, i.e. the current position of the economy in the business cycle and the current setting of the monetary conditions. The expected future evolution of equilibrium variables also provides a framework for the fundamental orientation of the forecast.

The key macroeconomic variables serving as the framework for the message of the forecast include potential output, equilibrium real interest rates and the equilibrium real exchange rate. Since the preparation of the last forecast, no information leading to a reassessment of their fundamental trends has come to light. As in April and January 2004, the forecast for 2004–2005 assumes a growth rate of potential output (i.e. the

non-accelerating inflation rate of output) of 2.5% to 3%, a one-year equilibrium real interest rate of around 1.5%, and a strengthening of the equilibrium real exchange rate at a pace of just under 3% at present, gradually falling to 2% at the end of 2006.

BOX
The exchange rate in the CNB's forecasting system

The relatively small and open Czech economy is strongly affected by external factors. These include changes in the prices of energy-producing raw materials and the economic situation of the Czech Republic's major trading partners. The koruna's exchange rate also plays an important role.

The CNB's overall macroeconomic forecast includes a forecast for the koruna-euro nominal exchange rate. In addition to the nominal exchange rate, which above all influences import prices, the real exchange rate – i.e. the exchange rate adjusted for changes in the price levels in the Czech Republic and the foreign economy in question – plays a vital role. The real exchange rate enters the forecast in the form of the exchange rate component of the monetary conditions (see the April 2004 Inflation Report), which equals the difference between the real exchange rate and its equilibrium value. The equilibrium value of the exchange rate at a given moment is the value that would be observed if the economy did not deviate from its equilibrium as a result of various larger or smaller shocks. The evolution of the equilibrium rate over time is determined by economic factors and lies beyond the reach of monetary policy, whereas the actual real (and nominal) exchange rate can be influenced by monetary policy instruments at least to some degree.

The equilibrium real exchange rate is not a directly measurable variable. However, we can assume, for instance, that it is close to the long-term trend of the actual real exchange rate. In practice, the trend of the relevant time series is often calculated using various "filtering methods", which "filter out" short-term fluctuations from the time series of the given variable. To estimate the equilibrium real exchange rate (as well as the equilibrium values of other variables), the CNB uses a multivariate filtering method known as the Kalman filter. This is a type of filtration based on information about the structure and operation of the economy. It thus incorporates a model of the linkages between the filtered variable and a number of other important macroeconomic variables (which is why we speak of a "multivariate" filter), therefore yielding better results than other, purely mathematical and univariate methods, which work only with the filtered variable itself. By including information about the structure of the linkages between the filtered variable and the rest of the economy, we eliminate, *inter alia*, the problems that arise at the ends of time series when using univariate filtering methods.

The central equation of the filtering approach used in the CNB's forecasting system assumes that the real exchange rate trend ($z\_eq_{t+4} - z\_eq_t$) corresponds to the trend in interest rates, namely the domestic 1Y PRIBOR (r_eq) and the foreign 1Y EURIBOR (r_eq^*). Moreover, the trend is adjusted for the risk premium ($prem\_eq$). In economics, the relation is generally referred to as real uncovered interest parity:

$$z\_eq_{t+4} - z\_eq_t = r\_eq_t^* - r\_eq_t + prem\_eq_t .$$

In addition to uncovered interest parity, the other starting points for estimating the long-term equilibrium real exchange rate are simulated scenarios of the convergence of the Czech economy towards the advanced European economies.

The current position of the economy in the business cycle is characterised by easy monetary conditions. In line with the last forecast, domestic real interest rates and the real exchange rate are both assessed as easy. However, the observed appreciation of the nominal exchange rate in 2004 Q2 led to a slower-than-forecasted easing of the real exchange rate. On the other hand, we regard the effect of the interest rate component of monetary conditions as easier, primarily as a result of slower growth in nominal interest rates in some segments of the financial market than expected in the April forecast and a temporary decline in German real interest rates.

When discussing the settings of the monetary conditions, we also take into account their past evolution and relation to the output gap, paying due heed to the expected lag in the transmission of the monetary conditions into economic activity. The forecast thus assumes that a gradual easing of the exchange rate component of the monetary conditions occurred during 2003. This easing caused the output gap, which reflects the overall impact of the demand environment on inflation in the forecast, to stop widening in late 2003/early 2004. In line with the April forecast, it subsequently closed somewhat in 2004 H1. The estimate for the negative output gap for 2004 Q2 is around -1.2%.

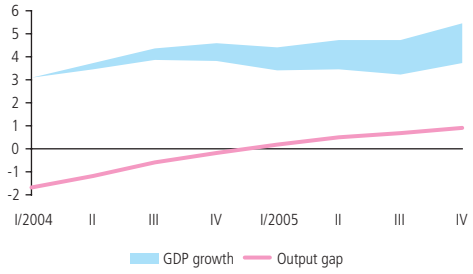
In addition to the mutual correspondence between the output gap and the monetary conditions, the assessment of the forecast's starting conditions must be in line with the observed development of the economy. The statistical data published during 2004 Q2 and discussed in the previous sections of this Report signal that the Czech economy remained below its potential. The somewhat slower growth in inflation than expected in the April forecast contributed to a moderate downscaling of both the initial output gap and its speed of closure. However, the slower growth in inflation was only partially reflected in slower closure of the output gap, since it can be partly explained by the evolution of food prices, in which the relationship between agricultural producer price inflation and food price inflation became less distinct. This was due to the different weights of the rising prices of some commodities in the agricultural producer price index and food price index. The forecast expects this slower transmission of commodities prices into food prices to continue.

The published data on GDP growth in 2004 Q1 confirmed the turnaround in economic activity foreseen in the April forecast. The moderate slowdown in consumption growth is consistent with the evolution of households' real disposable income and with the perception of a neutral interest rate component of the monetary conditions in 2003. The current evolution of consumer credit and M1 indicates continuing growth in household consumption at a similar pace in 2004 Q2. Growth in retail sales was slower than expected in Q2, but their relationship to consumption has recently become less clear-cut, so the forecast does not assign too much weight to the current data. In line with the April forecast, investment growth became the engine of economic growth, being even more buoyant than expected. The higher investment growth, however, resulted in faster import growth. The forecast for the contribution of net exports to GDP thus was not entirely fulfilled. The increase in investment activity is consistent with the perception of a gradual easing of the monetary conditions in 2003 H2. The change in the development of loans to non-financial corporations and in the structure of the money supply indicates a similar trend in investment activity in 2004 Q2 as well.

IV.3 THE MESSAGE OF THE FORECAST

The forecast continues to expect a turnaround in economic activity and a pick-up in economic growth in 2004. GDP growth will reach approximately 3.8% in 2004 and 4.2% in 2005. The prediction for potential output growth has been retained, so the output gap

Chart IV.1
ACCORDING TO THE FORECAST, THE CLOSING OUTPUT GAP WILL LEAD TO A PICK-UP IN GDP GROWTH IN 2004
(percentages)



should close quite quickly up to the beginning of 2005. During 2005, the output gap will attain positive values, according to the forecast. The reaching and exceeding of potential output should also bring about a turnaround in employment.

The pick-up in GDP growth reflects the easy monetary conditions and the onset of recovery abroad. An easing of the monetary conditions is expected in both the exchange rate and interest rate components. Moreover, the easing of the interest rate component of the monetary conditions should be sustained by a gradual increase in inflation and the related automatic pressure for a decline in real interest rates during 2004 as well. The evolution of the monetary conditions and the onset of the economic recovery abroad should be reflected in the GDP growth structure by a strengthening of the role of investment as the main factor of economic growth. According to the forecast, investment growth should gradually pick up speed, amounting to as much as 10% in mid-2005. This trend should be accompanied by a gradual rise in lending to non-financial corporations by the banking sector and by sustained high growth in housing loans to households.

According to the forecast, the growth in household consumption in 2004 will remain around 4%. This slowdown compared to 2003 should be due to slower growth in real disposable income and the lagged effect of the tightening of real interest rates during 2003. The falling growth in real disposable income stems from higher inflation than in 2003 coupled with a flat growth rate of aggregate nominal wages around 6%. In 2005 H2, however, the forecast is for a moderate rise in consumption expenditure growth, which corresponds – with the relevant lag – to the current easy interest rate component of the monetary conditions.

The economic recovery in 2004 and 2005 should also be accompanied by higher export activity, stemming – as in the case of investment activity – from the easy exchange rate and the gradual onset of economic recovery abroad. The fast growth in investment, however, brings with it an increase in investment imports. Thus, the growing exports should be balanced by higher imports, according to the forecast. This will result in an increase in foreign trade turnover, but net exports will not make a significant contribution to GDP growth. From the point of view of current prices, the foreign trade trend will be consistent with an improving output and trade balance in 2004 and 2005 thanks to favourable terms of trade.

The forecast is for gradual moderate appreciation of the nominal exchange rate from an initial CZK 32/EUR over the entire prediction horizon. The nominal exchange rate trend ensues from growth in the interest rate differential and a gradual decline in the risk premium. The appreciation of the nominal exchange rate since the preparation of the last forecast generates a lower import price forecast. Counteracting this trend, however, is a rise in some commodity prices and rising inflation abroad. Import price inflation therefore initially stays positive, but negative growth rates are expected for this indicator as from 2005. Compared to the last forecast, however, the import price trajectory is generally higher.

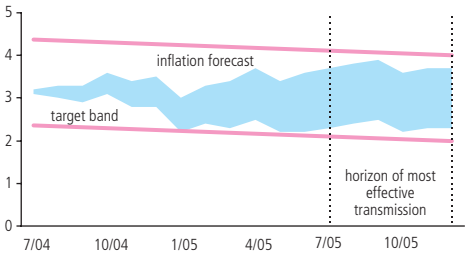
The aforementioned evolution of real economic activity, imported inflation and exogenous factors determines the future inflation profile. According to the current forecast, the closure of the output gap and its switch to positive figures, together with the resulting inflationary pressures, will start to emerge at the beginning of 2005, i.e. slightly later than predicted in the April forecast. The forecasted development of the individual components of GDP, in which faster growth in investment and exports is the major contributor to the closure of the output gap, is quite usual within the business cycle. Its impact on consumer prices can therefore be derived using the standard approach in the CNB's forecasting system based on the relationship between the aggregate output gap and inflation.

Inflation has been strongly affected in 2004 by changes to indirect taxes linked with accession to the EU and with the government's reform of public finances. Their effect on inflation corresponds for the most part to expectations, or is only slightly lower. Compared to the last forecast, the expected growth in food prices has declined. Lower price growth than in the April forecast is therefore predicted for the rest of 2004, reaching just above 3%. The outlook for adjusted inflation excluding fuels has also shifted downwards: adjusted inflation excluding fuels should grow by 2.6% in 2004 Q4.

The April forecast predicted a gradual unwinding of the effect of changes in indirect taxes during 2005. The current forecast, however, adds the expected rise in excise duties on cigarettes, which also results from the Czech Republic's accession to the EU, to the tax changes introduced in 2004. The forecast assumes that this rise will be implemented on 1 January 2005. The secondary impacts of this tax change are assessed in the forecast at the same level as in the case of the 2004 tax changes, i.e. as relatively limited. The expected tax changes thus alter to some degree the prediction for headline inflation in 2005 compared to the April forecast. However, the primary driving force behind the increase in inflation adjusted for these tax changes will be still rising demand-pull inflation, with the inflationary effect of the positive output gap being partly offset by declining import prices. Headline inflation will fluctuate around 3% in 2005 H2, i.e. near the centre of the inflation target.

Consistent with the July forecast and its assumptions is a moderately rising path of short-term interest rates, which is, however, slightly lower than in the April forecast. Like previous forecasts, this forecast assumes that monetary policy will not respond to the primary effects of the changes to indirect taxes included in the forecast, but will anticipate the secondary effects.[33]

Chart IV.2
THE INFLATION FORECAST IS AT THE CENTRE OF THE TARGET BAND AT THE HORIZON OF MOST EFFECTIVE TRANSMISSION
(annual consumer price inflation, percentages)



IV.4 EXPECTATIONS OF ECONOMIC AGENTS

The inflation outturns expected by financial market participants decreased slightly. Nevertheless, the analysts still expected inflation to rise somewhat in the immediate future, mainly because of the lingering effect of the VAT changes. Other inflationary factors included growth in agricultural production prices and wage growth in the public sector. Prices of oil and metals on world markets remained an external risk factor. According to financial market participants, inflation is thus set to peak some time in late Q3 or early Q4. A modest decline is expected thereafter. The inflation expectations of corporations also decreased, while those of households were unchanged.

The CNB also monitors inflation expectations at the three-year horizon. The expected figures lie in a narrower range. The price level is likely to be subject to the same influences as in the euro area countries. The inflation expectations of the financial market at this horizon are consistent with the CNB's medium-term target of 3%.

Expected interest rates increased in the period under review. For the immediate future most financial market participants were predicting a further rise in the CNB's key rates – by around 0.7 percentage point overall at the one-year horizon. The expectations of a rise in the CNB's interest rates, consistent with the interest rate path trend, were in line with the CNB forecast described above.

Table IV.2
THE INFLATION EXPECTATIONS OF ECONOMIC AGENTS TENDED TO FALL
(percentages)

	12/03	3/04	4/04	5/04	6/04
Consumer price index					
1Y horizon:					
Financial market	3.3	3.0	2.8	2.6	2.7
Corporations	2.9	3.3			3.1
Households	4.2	4.9			4.9
3Y horizon:					
Financial market	2.8	2.8	2.9	2.9	2.7
Corporations	2.8	3.1			3.0
Households	4.6	4.9			5.0
1Y PRIBOR					
1Y horizon:					
Financial market	3.1	3.1	2.9	3.2	3.5

33 In the current forecast, monetary policy also does not react to the direct secondary effects connected with the reduction in the basic VAT rate from 22% to 19%. The failure to fully reduce prices in relation to this change was assessed as structural given the negative output gap. However, this change is of only marginal importance to the message of the forecast.

ANNEX

THE CNB HAS FULLY INTEGRATED INTO THE EUROPEAN SYSTEM OF CENTRAL BANKS

Upon signing the Accession Treaty in April 2003, the acceding countries were granted the right to send observers to the majority of bodies and institutions of the European Union, to obtain source materials for meetings and to present their views. As of the Czech Republic's accession to the EU on 1 May 2004, the observers became full members. Certain bodies and committees of the European Commission and Council, and above all the committees of the European System of Central Banks (ESCB), address issues falling within the CNB's spheres of competence.

There are 12 committees in the ESCB covering the bank's various activities, namely:

1.	*Accounting and Monetary Income Committee*	AMICO
2.	*Banknote Committee*	BANCO
3.	*Banking Supervision Committee*	BSC
4.	*External Communications Committee*	ECCO
5.	*Internal Auditors Committee*	IAC
6.	*International Relations Committee*	IRC
7.	*Information Technology Committee*	ITC
8.	*Legal Committee*	LEGCO
9.	*Market Operations Committee*	MOC
10.	*Monetary Policy Committee*	MPC
11.	*Payment and Settlement Systems Committee*	PSSC
12.	*Statistics Committee*	STC

Some meetings of these committees are attended by representatives of all the ESCB countries, but in some cases only the euro area Member States attend. The CNB's representatives only attend the meetings of all countries. Most committees have several working groups, where the CNB is also represented by its experts.

The issues discussed in the committees and working groups often concern not only the body's area of specialisation, but overlap with the activities of other committees and working groups. Consequently, several CNB organisational units often work together in performing the CNB's tasks arising from ESCB meetings, and sometimes the CNB must also co-operate with other Czech administrative bodies. The CNB Bank Board is regularly informed about the activities of the CNB's representatives in ESCB bodies in a document compiled from the representatives' quarterly reports.

As regards monetary policy, the Monetary Policy Committee (MPC) and the International Relations Committee (IRC) are of key importance. The MPC deals with issues involving monetary policy strategy in euro area countries and EU Member States outside the euro area, using documents prepared by three working groups (on forecasting, econometric modelling and fiscal policy). It focuses on regular forecasting exercises, the preparedness of countries to enter the euro area, interactions between monetary and fiscal policy, and issues relating to the stability of financial systems.

The IRC deals with international co-operation and provides a platform for exchanging opinions in this area. The Committee's key activities divide into two areas. The first is co-operation with countries outside the EU – above all in preparing the opinions of the euro area/ESCB/ECB on negotiations with countries and international organisations concerning the monetary and foreign exchange system and on EMU-related issues. It also assesses the functioning of the international monetary system and international financial markets, including the balance of payments, international debt and the euro's international position, and evaluates the architecture of the international monetary system and the stability of international money markets. The second area is co-operation within the EU – periodic ERM II assessment, evaluation of applications for membership in ERM II and accession to the EU and the EMU, and co-operation with other European countries and institutions.

The work of the majority of ESCB committees is directed at preparing inputs for the meetings of the Governing Council or General Council of the ECB. The Governing Council consists of the members of the ECB's Executive Board (i.e. the President and Vice-President of the ECB and the four other members of the Board) and the governors of the national central banks from the 12 euro area countries. The Governing Council's primary responsibilities are to adopt the guidelines and take the

decisions necessary to ensure the performance of the tasks entrusted to the Eurosystem, and to formulate monetary policy for the euro area. This includes decisions relating to the ECB's monetary objectives, key interest rates and the supply of reserves in the Eurosystem. The Governing Council also approves guidelines for the implementation of those decisions.

The General Council has been established for a transitional period and, in accordance with the Statute of the ESCB and of the ECB, will be dissolved once the EU Member States have adopted the euro. The General Council carries out the tasks taken over from the former European Monetary Institute which the ECB is required to perform in Stage Three of Economic and Monetary Union on account of the fact that not all EU Member States have adopted the euro yet. It consists of the President and the Vice-President of the ECB and the governors of the national central banks, which means it currently has 27 members. Among other things, it is responsible for co-ordinating monetary policy in countries outside the euro area and for monitoring the operation of the ERM II. It also assesses fiscal policy developments in EU Member States.

In connection with the Czech Republic's membership in the EU, the CNB is also active in other bodies and institutions of the European Union, such as the European Commission (the Economic and Financial Committee, the Economic Policy Committee) and Eurostat, in addition to its activities within the ESCB.

MINUTES OF THE CNB BANK BOARD MEETINGS

MINUTES OF THE BOARD MEETING ON 29 APRIL 2004

Present at the meeting: Zdeněk Tůma (Governor), Oldřich Dědek (Vice-Governor), Michaela Erbenová (Chief Executive Director), Jan Frait (Chief Executive Director), Pavel Racocha (Chief Executive Director), Pavel Štěpánek (Chief Executive Director)

The Board opened the meeting with a presentation of the 4th situational report on economic and monetary development, and along with it, the new macroeconomic forecast.

The report emphasised the relaxed nature of monetary conditions, and in particular, the exchange rate component. In relation to relaxed monetary conditions in the past, the worsening tendency of the negative output gap had ended. Developments in Q1 showed that the low-inflation environment, which was characteristic of economies performing below their growth potential, still existed.

In view of more relaxed monetary conditions than in the previous macroeconomic forecast, faster economic growth was expected. The newly available data for 2003 indicated that fiscal policy's growth input was lower than originally expected. The contribution of foreign trade should increase growth, as was also indicated by certain preliminary data for Q1. The share of investments was expected to increase as well, backed by the improved financial situation of companies.

Inflation pressures associated with the closing output gap and its gradual shift to positive values would start to have a larger impact as early as the end of this year. It was assumed that the corresponding reaction of food prices to the rise in agricultural producer prices had not yet taken full effect. In addition, rising oil prices were still expected to affect the related price groups. The higher estimate for the secondary effects of indirect tax changes was also a change from the last forecast.

These factors would cause a shift in the inflation forecast to a level of about 4% year-on-year CPI growth by the end of this year. In the second half of 2005, inflation should fluctuate in the centre of the targeted band, i.e. around 3% of the year-on-year CPI. The gradual rise in interest rates was consistent with the new macroeconomic forecast.

In addition to the baseline scenario, two alternative scenarios were also included in the situational report. These scenarios described macroeconomic and price development in the event of more serious deviations from the base forecast. The first alternative discussed the various levels of impact, i.e. higher or lower, that inflation expectations would have in relation to indirect tax adjustments, which affected the level of interest rates consistent with the forecast by about + 0.5 percentage points. The second alternative scenario was based on the assumption of a stronger koruna exchange rate vis-à-vis the euro, and this scenario would end near the CNB's January forecast.

Following the presentation of the situational report, board members turned to a discussion on the positioning of the new forecast, which substantially shifted expected economic growth and inflation upwards in 2004. The Board considered the new data on the structure of 2003 GDP growth to be important. The realisation that the weight of non-fiscal factors was higher than previously expected was accepted as one of the basic arguments in favour of dynamic GDP growth in the future.

It was said that global economic recovery generated by developments in the USA and China had no discernablediscernible effect so far on demand growth and inflation pressures in the European Economic Area. Uncertainty related to the speed and vigour of recovery for the Czech Republic's main business partners was indicated as the main forecast risk. In this respect, the absence of relevant Q1 data was mentioned as a reminder. One view expressed that forward-looking monetary policy was based on the analysis of long-term trends, and an ex post reaction to any additional information would create the risk of delayed decision-making.

Although an amendment to the VAT Act was passed, continued uncertainty was not only the immediate secondary effect, but above all, it involved longer-term consequences which were influenced by inflation expectations, and monetary policy must respond to them.

There was consensus among board members that a moderately prevailing risk for the new forecast was the likelihood of lower inflation as well as lower economic growth. The Board confirmed that the gradual rise in interest rates was consistent with the forecast's baseline scenario. In the light of this situation, the Board pointed to the unsustainability of negative real interest rates in the long run, especially in a phase of economic recovery.

At the close of the meeting and following the discussion on the situational report, the Board decided unanimously to leave the CNB two-week repo rate unchanged at 2%.

MINUTES OF THE BOARD MEETING ON 27 MAY 2004

Present at the meeting: Zdeněk Tůma (Governor), Oldřich Dědek (Vice-Governor), Luděk Niedermayer (Vice-Governor), Michaela Erbenová (Chief Executive Director), Jan Frait (Chief Executive Director), Pavel Štěpánek (Chief Executive Director)

The Board opened the meeting with a presentation of the May situational report assessing the new information and risks associated with the April macroeconomic forecast.

April consumer inflation was slightly lower than was originally predicted in April due to accumulation of certain deviations within individual inflation segments. On the contrary, production – industrial and agricultural producer prices - rose at a slightly faster pace than predicted. Agricultural producer prices showed accentuated dynamics in the last few months, which, however, did not reflect in the food prices. Import prices were slightly higher in March than forecasted. External environment predictions were not significantly amended during the last month, with the exception of increased oil price estimates, as these reflected the unfavourable situation on the world markets.

The real economy figures, especially industrial and construction production indicated increased economic growth, which should according to the forecast be due to the revival of investment activity and increased export dynamics. The slowing down pace of retail sales in the first quarter was consistent with already forecasted expectations of the deceleration of consumer demand dynamics. The situation on the labour market was from the standpoint of the unemployment rate as well as the employment indicators in principle consistent with the forecast. M2 growth kept accelerating in March, however, dynamics of lending growth did not increase. The trade deficit for the first four months was sluggish in year-on-year nominal terms, although the balance in March and April was worse than predicted.

Following the presentation of the situational report, board members turned to a discussion on the risks of the April forecast fulfilment. The Board agreed that the new data gave no reason to change the overall view of the economic situation. In consistency with the April board meeting, the risks of the forecast were in relation to the inflation as well as from the economic growth standpoint shifted downwards.

When discussing economic growth there was an overall consensus that it was accelerating. It was repeatedly said that the risk of the forecast could be the different recovery structure in the sense of lower net export and private consumption contribution, which could be compensated by faster investment dynamics. An assumption was made that this development could be related to the lower demand inflation pressures. It was, however, also said that there was not enough empirical evidence to support this theory. The risk in relation to net exports was repeatedly found in an uncertain foreign demand perspective, especially in Europe. A different growth structure could also reflect the CZK exchange rate development vis-à-vis the euro, which was moving in stronger values against the forecast assumptions. In connection with domestic economic recovery it was also said that its risk could be the low flexibility of the supply side of the economy.

From the viewpoint of pro-inflationary pressures the attention was focused especially on cost factors. The Board agreed that the assessment of the risks resulting from oil price growth in relation to inflation and economic growth could be very difficult. For the short-term outlook the high oil prices signified a pro-inflationary risk. The possible persistent oil-price shock could however in the longer term weaken the world's prosperity, which should in the end lower the domestic inflation growth pressures. On the other hand there was an opinion, that due to the improved structure of economies the global resistance against the oil shock was higher than in past decades.

Apart from oil, agriculture producer prices were also discussed. It was said that its dynamic growth compensated on most levels the sifting of the price level in the past years and that the effect on food prices was limited. It was, however, mentioned that agriculture producer price growth could be influenced by new circumstances associated with the opening of the European agricultural market after the Czech Republic's EU accession.

Fiscal policy was also discussed. It was said that not only monetary but also fiscal policies were both responsible for sustaining a stable economic environment in the closing output gap situation. A concern was expressed that higher tax income caused by the acceleration of economic growth could be used for additional pro-cyclical spending, which would weaken the structural scope of fiscal consolidation. Cautious fiscal policy was also important because as of this year the fiscal system should be facing uncertainties connected with the budgetary effects of the financial flows between the Czech Republic and the EU.

At the close of the meeting the Board decided by a majority vote to leave the CNB two-week repo rate unchanged at 2%. Five members voted in favour of this decision, and one member voted for increasing rates by 0.25 of a percentage point.

MINUTES OF THE BOARD MEETING ON 24 JUNE 2004

Present at the meeting: Zdeněk Tůma (Governor), Luděk Niedermayer (Vice-Governor), Michaela Erbenová (Chief Executive Director), Pavel Racocha (Chief Executive Director), Pavel Štěpánek (Chief Executive Director)

The Board opened the meeting with a presentation of the June situational report assessing the new information and risks associated with the April macroeconomic forecast.

May CPI growth was a little lower than was originally predicted in April. A slight downward deviation was seen not only in net inflation but also in the segments of regulated prices. Food prices continued to show lower growth than the forecast. On the other hand, adjusted inflation rose at a somewhat faster pace in May due to fuel prices. Production price development was faster in May than the assumptions in the April forecast. As far as industrial prices go, these mainly reflect the effect of world metal price growth. This factor influenced import prices, which were slightly higher in April contrary to the forecast. Newly available information about the external economic environment led to a slight pro-inflationary adjustment, especially in the area of producer and consumer prices in Germany this year.

The economic growth attained in the first quarter was in line with the April forecast. With regards to its structure, the slowdown in the household consumption prediction was fulfilled. Poorer-than-forecasted net exports and government consumption development was compensated with accelerated investment dynamics. Industrial production development in April shows continued economic growth. April construction output was significantly influenced by the May VAT increase. In the next several months, a temporary year-on-year decline in construction production could be expected. The situation on the labour market in May was, in principle, consistent with the forecast. Wage development in the first quarter was faster than predicted in April, especially in the non-business sector, where the time-scale seasonality change would take place in connection with implementing a 16-scale tariff and with respect to resolving the issue of 13th and 14th salaries. M2 growth kept accelerating in April, as did lending growth.

Following the presentation of the situational report, board members discussed the new economic data and risks associated with the April forecast.

The majority of the Board agreed that, in principle, the newly available data confirmed the positioning of the April forecast, which expected economic growth pulled by investment activity and higher exports. Gradual interest rate growth was also consistent with the forecast for April, even in the case of CZK exchange rate development vis-à-vis the euro according to the alternative appreciated scenario. Some board members pointed out the somewhat, rather different structure of economic growth, in particular, slower export growth. It was also said that the revision of the national accounts, which is currently under way could increase the uncertainty regarding the past and present development of GDP and the output gap.

The Board also focused its attention on the interpretation of the one-off effect of the Czech Republic's EU entry on short-term economic indicators, especially gross fixed capital formation development in the first quarter and also the outcome of construction production in April and the most likely development of this indicator in the next few months. It should be expected that some short-term indicators could show some major fluctuations over the next several months, which would complicate the assessment of economic development.

Further discussed were the causes of existing inflation deviations from the April forecast. The Board agreed that, for the time being, no straightforward explanation existed for why inflation had reached slightly lower values than predicted, despite the stronger pro-inflationary cost pressures. This could be due to a combination of factors such as a more open initial negative output gap, easing of the links between cost factors and consumer prices, or the increase of already high competition on the domestic market. The more gradual time distribution of the primary effects of the indirect tax increase could also play a role.

On the other hand, it was repeatedly said that despite these uncertainties, total as well as net year-on-year inflation were increasing. It was said that faster wage growth and even household lending dynamics could experience a lower consumption rate decline than predicted. Attention was also drawn to the fact that long-term negative real interest rates are not adequate in a scenario of growing inflation and continuing economic growth.

At the close of the meeting the Board decided by a majority vote to increase the CNB two-week repo rate by 0.25 percentage points to 2.25%, effective 25 June 2004. The Board also increased the discount rate and Lombard rate by the same amount to 1.25% and 3.25%, respectively. Three members voted in favour of this decision, and two members voted for leaving rates unchanged.

INFLATION DEVELOPMENT

annual percentage changes

	1	2	3	4	5	6	7	8	9	10	11	12
2000												
Consumer prices	3.4	3.7	3.8	3.4	3.7	4.1	3.9	4.1	4.1	4.4	4.3	4.0
Regulated prices	7.3	7.3	7.3	7.4	7.5	7.8	6.9	7.0	7.0	7.2	7.3	7.3
(contribution to consumer price inflation)	*1.94*	*1.95*	*1.96*	*1.98*	*1.99*	*2.09*	*1.87*	*1.90*	*1.91*	*1.98*	*1.99*	*1.97*
Influence of indirect tax growth on unregulated prices												
(contribution to consumer price inflation)	*0.32*	*0.32*	*0.32*	*0.14*	*0.14*	*0.14*	*-0.18*	*-0.18*	*-0.18*	*-0.18*	*-0.18*	*-0.18*
Net inflation	1.6	1.9	2.1	1.7	2.1	2.6	3.1	3.2	3.2	3.5	3.4	3.0
(contribution to consumer price inflation)	*1.19*	*1.38*	*1.55*	*1.27*	*1.57*	*1.90*	*2.25*	*2.36*	*2.35*	*2.57*	*2.49*	*2.16*
of which: prices of food, beverages and tobacco	-0.6	0.0	0.1	-0.4	0.2	0.4	1.6	2.5	2.8	3.9	3.9	3.6
(contribution to consumer price inflation)	*-0.16*	*0.00*	*0.02*	*-0.12*	*0.07*	*0.13*	*0.45*	*0.73*	*0.79*	*1.06*	*1.06*	*1.01*
adjusted inflation	3.1	3.2	3.5	3.2	3.4	4.0	4.1	3.8	3.5	3.4	3.2	2.6
(contribution to consumer price inflation)	*1.35*	*1.39*	*1.53*	*1.39*	*1.49*	*1.77*	*1.80*	*1.63*	*1.56*	*1.51*	*1.43*	*1.15*
Inflation rate (annual moving average)	2.1	2.2	2.3	2.4	2.5	2.6	2.9	3.1	3.3	3.6	3.8	3.9
2001												
Consumer prices	4.2	4.0	4.1	4.6	5.0	5.5	5.9	5.5	4.7	4.4	4.2	4.1
Regulated prices	10.3	10.4	10.6	10.8	10.7	10.4	11.5	11.8	11.9	11.8	11.7	11.7
(contribution to consumer price inflation)	*1.95*	*1.98*	*2.01*	*1.98*	*2.00*	*1.97*	*2.12*	*2.19*	*2.19*	*2.19*	*2.16*	*2.17*
Influence of indirect tax growth on unregulated prices												
(contribution to consumer price inflation)	*-0.18*	*-0.18*	*-0.18*	*0.00*	*0.00*	*0.00*	*0.01*	*0.01*	*0.05*	*0.05*	*0.05*	*0.05*
Net inflation	3.0	2.9	2.9	3.3	3.8	4.4	4.7	4.1	3.1	2.7	2.4	2.4
(contribution to consumer price inflation)	*2.37*	*2.23*	*2.24*	*2.62*	*2.97*	*3.52*	*3.74*	*3.31*	*2.54*	*2.15*	*1.98*	*1.92*
of which: prices of food, beverages and tobacco	3.8	3.5	4.2	5.5	6.0	7.7	6.9	5.1	4.0	2.9	2.6	2.9
(contribution to consumer price inflation)	*1.09*	*1.02*	*1.25*	*1.62*	*1.78*	*2.24*	*2.11*	*1.70*	*1.28*	*0.97*	*0.87*	*0.80*
adjusted inflation	2.5	2.4	2.0	1.9	2.3	2.4	3.2	3.4	2.5	2.4	2.3	2.1
(contribution to consumer price inflation)	*1.28*	*1.21*	*0.99*	*1.00*	*1.18*	*1.27*	*1.63*	*1.62*	*1.26*	*1.17*	*1.11*	*1.12*
Inflation rate (annual moving average)	4.0	4.0	4.0	4.1	4.2	4.3	4.5	4.6	4.7	4.7	4.7	4.7
2002												
Consumer prices	3.7	3.9	3.7	3.2	2.5	1.2	0.6	0.6	0.8	0.6	0.5	0.6
Regulated prices	7.6	8.1	8.0	6.5	6.3	6.3	5.3	5.0	4.9	3.4	3.4	3.3
(contribution to consumer price inflation)	*1.49*	*1.60*	*1.59*	*1.28*	*1.24*	*1.22*	*1.05*	*0.98*	*0.98*	*0.69*	*0.69*	*0.66*
Influence of indirect tax growth on unregulated prices												
(contribution to consumer price inflation)	*0.05*	*0.05*	*0.05*	*0.05*	*0.05*	*0.05*	*0.05*	*0.05*	*0.00*	*0.00*	*0.00*	*0.00*
Net inflation	2.7	2.7	2.5	2.4	1.5	-0.1	-0.6	-0.6	-0.3	-0.1	-0.2	-0.2
(contribution to consumer price inflation)	*2.20*	*2.15*	*2.01*	*1.89*	*1.20*	*-0.12*	*-0.47*	*-0.46*	*-0.22*	*-0.11*	*-0.18*	*-0.15*
of which: prices of food, beverages and tobacco	3.2	3.0	2.3	1.7	0.6	-2.6	-3.6	-3.5	-2.9	-3.0	-3.2	-3.4
(contribution to consumer price inflation)	*0.88*	*0.82*	*0.65*	*0.47*	*0.16*	*-0.72*	*-0.97*	*-0.96*	*-0.79*	*-0.80*	*-0.87*	*-0.93*
adjusted inflation	2.5	2.5	2.6	2.7	2.0	1.1	0.9	0.9	1.1	1.3	1.3	1.5
(contribution to consumer price inflation)	*1.32*	*1.33*	*1.37*	*1.43*	*1.04*	*0.60*	*0.50*	*0.50*	*0.56*	*0.69*	*0.69*	*0.79*
Inflation rate (annual moving average)	4.6	4.6	4.6	4.5	4.3	3.9	3.5	3.1	2.7	2.4	2.1	1.8
2003												
Consumer prices	-0.4	-0.4	-0.4	-0.1	0.0	0.3	-0.1	-0.1	0.0	0.4	1.0	1.0
Regulated prices	-0.3	-0.8	-0.8	1.4	1.5	1.5	0.4	0.4	0.4	1.2	1.2	1.3
(contribution to consumer price inflation)	*-0.07*	*-0.15*	*-0.16*	*0.29*	*0.31*	*0.32*	*0.08*	*0.09*	*0.08*	*0.24*	*0.24*	*0.27*
Influence of indirect tax growth on unregulated prices												
(contribution to consumer price inflation)	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*
Net inflation	-0.4	-0.2	-0.2	-0.5	-0.4	0.0	-0.2	-0.1	0.0	0.3	0.9	1.0
(contribution to consumer price inflation)	*-0.32*	*-0.17*	*-0.15*	*-0.38*	*-0.30*	*-0.01*	*-0.19*	*-0.10*	*-0.01*	*0.20*	*0.70*	*0.77*
of which: prices of food, beverages and tobacco	-4.1	-3.8	-3.5	-3.5	-2.8	-1.0	-0.9	-0.9	-0.1	0.6	2.5	2.7
(contribution to consumer price inflation)	*-1.06*	*-1.06*	*-0.97*	*-0.94*	*-0.76*	*-0.28*	*-0.22*	*-0.22*	*-0.04*	*0.16*	*0.66*	*0.70*
adjusted inflation	1.5	1.7	1.5	1.1	0.9	0.5	0.1	0.2	0.0	0.1	0.1	0.1
(contribution to consumer price inflation)	*0.74*	*0.89*	*0.82*	*0.56*	*0.46*	*0.27*	*0.04*	*0.12*	*0.02*	*0.04*	*0.04*	*0.06*
Inflation rate (annual moving average)	1.5	1.1	0.8	0.5	0.3	0.2	0.2	0.1	0.0	0.0	0.1	0.1
2004												
Consumer prices	2.3	2.3	2.5	2.3	2.7	2.9						
Regulated prices	5.0	4.9	4.7	3.1	2.4	2.4						
(contribution to consumer price inflation)	*1.01*	*0.99*	*0.96*	*0.63*	*0.49*	*0.49*						
Influence of indirect tax growth on unregulated prices												
(contribution to consumer price inflation)	*0.35*	*0.35*	*0.35*	*0.39*	*0.61*	*0.68*						
Net inflation	1.2	1.2	1.4	1.5	2.0	2.1						
(contribution to consumer price inflation)	*0.96*	*0.92*	*1.15*	*1.21*	*1.63*	*1.71*						
of which: prices of food, beverages and tobacco	2.8	2.8	3.2	3.3	3.4	2.7						
(contribution to consumer price inflation)	*0.75*	*0.75*	*0.83*	*0.86*	*0.89*	*0.71*						
adjusted inflation	0.4	0.3	0.6	0.6	1.4	1.9						
(contribution to consumer price inflation)	*0.21*	*0.17*	*0.32*	*0.35*	*0.74*	*1.00*						
Inflation rate (annual moving average)	0.3	0.5	0.8	1.0	1.2	1.4						

CNB calculation based on CZSO data

INFLATION DEVELOPMENT

monthly percentage changes

	1	2	3	4	5	6	7	8	9	10	11	12
	2000											
Consumer prices	1.7	0.2	0.0	-0.1	0.2	0.6	0.6	0.2	0.0	0.3	0.1	0.2
Regulated prices	4.8	0.1	0.1	0.2	0.1	0.4	1.0	0.1	0.1	0.2	0.1	0.1
(contribution to consumer price inflation)	*1.29*	*0.04*	*0.02*	*0.05*	*0.02*	*0.10*	*0.27*	*0.02*	*0.03*	*0.06*	*0.03*	*0.01*
Influence of indirect tax growth on unregulated prices												
(contribution to consumer price inflation)	*0.00*	*0.00*	*0.00*	*-0.18*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*
Net inflation	0.6	0.2	0.0	0.0	0.3	0.7	0.5	0.2	-0.1	0.3	0.1	0.2
(contribution to consumer price inflation)	*0.42*	*0.13*	*-0.01*	*-0.01*	*0.21*	*0.48*	*0.34*	*0.18*	*-0.08*	*0.26*	*0.10*	*0.14*
of which: prices of food, beverages and tobacco	1.0	0.1	-0.6	-0.5	0.3	0.4	-0.1	0.7	0.3	1.1	0.3	0.6
(contribution to consumer price inflation)	*0.30*	*0.03*	*-0.17*	*-0.14*	*0.07*	*0.11*	*-0.02*	*0.20*	*0.08*	*0.29*	*0.08*	*0.16*
adjusted inflation	0.3	0.2	0.3	0.3	0.3	0.8	0.8	0.0	-0.4	-0.1	0.0	0.0
(contribution to consumer price inflation)	*0.12*	*0.10*	*0.15*	*0.13*	*0.14*	*0.37*	*0.36*	*-0.02*	*-0.15*	*-0.04*	*0.02*	*-0.02*
	2001											
Consumer prices	1.9	0.0	0.1	0.4	0.6	1.0	1.0	-0.2	-0.7	0.0	-0.1	0.1
Regulated prices	7.7	0.3	0.2	0.3	0.0	0.1	2.1	0.3	0.2	0.1	0.0	0.0
(contribution to consumer price inflation)	*1.43*	*0.05*	*0.05*	*0.06*	*0.00*	*0.01*	*0.41*	*0.06*	*0.04*	*0.03*	*-0.01*	*0.01*
Influence of indirect tax growth on unregulated prices												
(contribution to consumer price inflation)	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.01*	*0.00*	*0.05*	*0.00*	*0.00*	*0.00*
Net inflation	0.6	0.0	0.0	0.4	0.8	1.3	0.7	-0.3	-1.0	-0.1	-0.1	0.2
(contribution to consumer price inflation)	*0.45*	*0.01*	*-0.01*	*0.31*	*0.57*	*1.07*	*0.56*	*-0.21*	*-0.82*	*-0.10*	*-0.05*	*0.10*
of which: prices of food, beverages and tobacco	1.2	-0.2	0.1	0.7	0.8	2.0	-0.9	-1.0	-0.8	0.0	0.0	0.9
(contribution to consumer price inflation)	*0.33*	*-0.06*	*0.03*	*0.19*	*0.23*	*0.56*	*-0.24*	*-0.27*	*-0.21*	*0.00*	*-0.01*	*0.24*
adjusted inflation	0.2	0.1	-0.1	0.2	0.7	1.0	1.5	0.1	-1.2	-0.2	-0.1	-0.3
(contribution to consumer price inflation)	*0.12*	*0.07*	*-0.04*	*0.12*	*0.34*	*0.51*	*0.81*	*0.06*	*-0.62*	*-0.10*	*-0.03*	*-0.14*
	2002											
Consumer prices	1.5	0.2	-0.1	-0.1	-0.1	-0.3	0.5	-0.2	-0.5	-0.3	-0.2	0.2
Regulated prices	3.7	0.8	0.2	-1.1	-0.1	0.0	1.1	0.0	0.1	-1.3	0.0	-0.1
(contribution to consumer price inflation)	*0.75*	*0.16*	*0.04*	*-0.23*	*-0.03*	*0.00*	*0.23*	*-0.01*	*0.03*	*-0.26*	*0.00*	*-0.02*
Influence of indirect tax growth on unregulated prices												
(contribution to consumer price inflation)	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*
Net inflation	0.9	0.0	-0.2	0.2	-0.1	-0.3	0.3	-0.2	-0.7	0.0	-0.1	0.2
(contribution to consumer price inflation)	*0.74*	*-0.03*	*-0.14*	*0.20*	*-0.11*	*-0.24*	*0.20*	*-0.19*	*-0.58*	*0.01*	*-0.11*	*0.13*
of which: prices of food, beverages and tobacco	1.5	-0.4	-0.5	0.1	-0.3	-1.2	-1.9	-1.0	-0.1	0.0	-0.3	0.7
(contribution to consumer price inflation)	*0.41*	*-0.11*	*-0.14*	*0.01*	*-0.08*	*-0.32*	*-0.50*	*-0.25*	*-0.03*	*-0.01*	*-0.08*	*0.18*
adjusted inflation	0.6	0.2	0.0	0.3	-0.1	0.2	1.3	0.1	-1.0	0.0	-0.1	-0.1
(contribution to consumer price inflation)	*0.33*	*0.08*	*0.00*	*0.18*	*-0.04*	*0.08*	*0.70*	*0.07*	*-0.56*	*0.02*	*-0.03*	*-0.05*
	2003											
Consumer prices	0.6	0.2	-0.1	0.2	0.0	0.0	0.1	-0.2	-0.5	0.1	0.5	0.2
Regulated prices	0.1	0.3	0.2	1.1	-0.1	0.0	0.0	0.0	0.1	-0.4	0.0	0.0
(contribution to consumer price inflation)	*0.03*	*0.06*	*0.03*	*0.23*	*-0.01*	*0.01*	*0.00*	*0.00*	*0.01*	*-0.09*	*0.00*	*0.00*
Influence of indirect tax growth on unregulated prices												
(contribution to consumer price inflation)	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*	*0.00*
Net inflation	0.7	0.2	-0.2	0.0	0.0	0.1	0.0	-0.1	-0.6	0.3	0.5	0.3
(contribution to consumer price inflation)	*0.55*	*0.14*	*-0.13*	*-0.03*	*-0.04*	*0.05*	*0.03*	*-0.11*	*-0.49*	*0.22*	*0.39*	*0.20*
of which: prices of food, beverages and tobacco	0.8	-0.2	-0.2	0.1	0.4	0.6	-1.7	-1.0	0.6	0.7	1.6	0.8
(contribution to consumer price inflation)	*0.22*	*-0.05*	*-0.05*	*0.04*	*0.10*	*0.16*	*-0.44*	*-0.25*	*0.16*	*0.18*	*0.42*	*0.22*
adjusted inflation	0.6	0.3	-0.1	-0.1	-0.3	-0.2	0.9	0.3	-1.2	0.1	-0.1	0.0
(contribution to consumer price inflation)	*0.33*	*0.18*	*-0.07*	*-0.06*	*-0.14*	*-0.11*	*0.47*	*0.15*	*-0.65*	*0.03*	*-0.03*	*-0.02*
	2004											
Consumer prices	1.8	0.2	0.1	0.0	0.4	0.2						
Regulated prices	3.7	0.2	0.0	-0.5	-0.7	0.0						
(contribution to consumer price inflation)	*0.76*	*0.04*	*0.01*	*-0.10*	*-0.15*	*0.00*						
Influence of indirect tax growth on unregulated prices												
(contribution to consumer price inflation)	*0.35*	*0.00*	*0.00*	*0.04*	*0.23*	*0.07*						
Net inflation	0.9	0.1	0.1	0.0	0.5	0.1						
(contribution to consumer price inflation)	*0.74*	*0.09*	*0.10*	*0.03*	*0.37*	*0.12*						
of which: prices of food, beverages and tobacco	1.0	-0.2	0.1	0.3	0.5	-0.1						
(contribution to consumer price inflation)	*0.26*	*-0.05*	*0.02*	*0.07*	*0.14*	*-0.03*						
adjusted inflation	0.9	0.3	0.1	-0.1	0.4	0.3						
(contribution to consumer price inflation)	*0.48*	*0.14*	*0.08*	*-0.04*	*0.23*	*0.14*						

CNB calculation based on CZSO data

CONSUMER PRICES

percentage changes; December 1999 = 100

Group	Constant 1999 weights in per mille	Months												Average since start of year
		1	2	3	4	5	6	7	8	9	10	11	12	
Total - 2000	1000.0	1.8	2.0	2.0	1.9	2.1	2.7	3.3	3.5	3.5	3.8	3.9	4.1	2.9
Total - 2001	1000.0	6.1	6.1	6.2	6.6	7.2	8.3	9.4	9.2	8.4	8.4	8.3	8.4	7.7
Food and non-alcoholic beverages	197.6	6.0	5.5	5.5	6.4	7.5	10.5	9.2	7.7	6.7	6.6	6.5	7.9	7.2
Alcoholic beverages and tobacco	79.2	3.4	3.9	4.3	4.6	4.9	5.0	4.9	4.9	5.2	5.5	5.6	5.4	4.8
Clothing and footwear	56.9	-3.3	-4.0	-4.0	-3.8	-3.7	-3.7	-3.9	-4.4	-4.4	-4.1	-3.8	-3.9	-3.9
Housing, water, electricity, gas and other fuels	236.4	14.2	14.4	14.6	14.8	15.1	15.4	18.4	18.6	18.8	18.9	19.0	19.0	16.8
Furnishings, household equipment and routine maintenance of the house	67.9	-0.6	-0.6	-0.5	-0.5	-0.5	-0.4	-0.4	-0.4	-0.4	-0.2	-0.3	-0.4	-0.4
Health	14.3	4.7	4.9	5.1	5.3	5.4	5.7	6.5	7.5	8.6	8.9	8.3	8.4	6.6
Transport	101.4	4.9	4.8	4.7	5.8	7.5	8.7	8.2	7.6	7.8	6.5	5.3	3.4	6.3
Communications	22.5	7.2	7.1	7.1	7.0	6.8	6.7	6.6	6.5	6.0	5.9	5.8	5.7	6.5
Recreation and culture	95.5	2.7	3.4	2.9	2.3	3.3	7.0	13.7	15.3	7.1	6.5	6.8	7.2	6.5
Education	4.5	3.4	3.4	3.5	3.5	3.5	3.6	3.6	3.6	6.7	6.8	6.8	6.8	4.6
Hotels, cafés and restaurants	74.2	3.1	3.6	3.3	3.7	4.0	4.1	4.2	4.4	5.2	5.5	5.7	5.9	4.4
Miscellaneous goods and services	49.5	5.0	5.5	6.2	7.3	7.4	7.4	7.7	7.6	7.8	8.4	8.6	8.7	7.3
Total - 2002	1000.0	10.0	10.2	10.1	10.0	9.9	9.6	10.1	9.9	9.3	9.0	8.8	9.0	9.7
Food and non-alcoholic beverages	197.6	10.0	9.4	8.7	8.3	7.8	6.0	3.2	1.7	1.5	1.4	1.0	2.1	5.1
Alcoholic beverages and tobacco	79.2	5.8	5.8	5.6	6.8	7.0	7.0	7.1	7.3	7.4	7.5	7.4	7.1	6.8
Clothing and footwear	56.9	-4.7	-5.5	-5.7	-5.7	-5.7	-5.8	-6.4	-7.4	-7.4	-7.4	-7.4	-7.7	-6.4
Housing, water, electricity, gas and other fuels	236.4	23.5	23.6	23.7	22.6	22.6	22.6	24.9	25.0	25.0	24.2	24.3	24.3	23.9
Furnishings, household equipment and routine maintenance of the house	67.9	-0.4	-0.5	-0.3	-0.3	-0.3	-0.4	-0.5	-0.7	-0.7	-0.8	-0.9	-1.0	-0.6
Health	14.3	9.2	9.7	10.1	10.2	10.9	11.2	12.9	13.1	13.3	13.0	12.8	12.8	11.6
Transport	101.4	3.0	3.0	3.3	5.5	5.1	4.7	4.1	3.9	5.1	4.9	4.6	4.1	4.3
Communications	22.5	6.0	11.4	11.3	11.3	9.9	9.9	11.1	11.0	11.6	9.4	9.3	8.2	10.0
Recreation and culture	95.5	7.4	8.5	7.9	7.2	7.0	8.4	13.8	15.2	7.3	7.2	7.0	7.2	8.7
Education	4.5	6.9	7.0	7.0	7.0	7.0	7.0	7.0	7.0	10.7	11.3	11.3	11.3	8.4
Hotels, cafés and restaurants	74.2	6.4	7.0	7.4	7.9	8.0	8.2	8.4	8.4	8.5	8.6	8.6	8.7	8.0
Miscellaneous goods and services	49.5	11.0	11.2	11.3	11.6	11.6	11.5	11.5	11.4	11.7	11.9	12.0	11.9	11.6
Total - 2003	1000.0	9.6	9.8	9.7	9.9	9.9	9.9	10.0	9.8	9.3	9.4	9.9	10.1	9.8
Food and non-alcoholic beverages	197.6	3.1	2.8	2.5	2.7	3.2	4.2	1.7	0.3	1.1	2.2	4.4	5.7	2.8
Alcoholic beverages and tobacco	79.2	7.6	7.7	7.7	7.7	7.9	7.6	7.7	7.7	7.9	7.7	8.0	7.8	7.8
Clothing and footwear	56.9	-9.1	-10.0	-10.4	-10.1	-10.1	-10.4	-11.5	-12.6	-12.4	-12.1	-11.9	-11.9	-11.0
Housing, water, electricity, gas and other fuels	236.4	24.9	25.3	25.4	26.5	26.6	26.6	26.9	27.0	27.0	26.6	26.6	26.6	26.3
Furnishings, household equipment and routine maintenance of the house	67.9	-1.1	-1.2	-1.4	-1.6	-1.8	-2.1	-2.3	-2.6	-2.7	-2.8	-3.0	-3.0	-2.1
Health	14.3	13.7	14.2	14.8	15.4	16.3	16.4	17.4	17.5	17.5	16.9	16.3	16.4	16.1
Transport	101.4	4.7	5.2	5.8	5.5	4.5	3.8	3.5	3.8	4.3	4.0	3.7	3.6	4.4
Communications	22.5	7.9	8.9	8.8	9.0	7.5	7.4	7.4	7.4	7.3	7.3	7.3	7.2	7.8
Recreation and culture	95.5	8.5	9.6	8.5	7.7	7.1	7.0	12.5	14.3	6.1	6.3	6.2	6.1	8.3
Education	4.5	11.3	11.4	11.5	11.5	11.5	11.6	11.6	11.6	11.0	12.0	12.0	12.0	11.6
Hotels, cafés and restaurants	74.2	9.2	9.4	9.4	9.5	9.6	9.6	9.9	10.0	10.3	10.5	10.7	10.8	9.9
Miscellaneous goods and services	49.5	14.0	14.6	14.7	14.7	14.6	14.6	14.5	14.7	14.9	15.4	15.3	15.2	14.8
Total - 2004	1000.0	12.1	12.3	12.4	12.4	12.9	13.1							12.5
Food and non-alcoholic beverages	197.6	7.4	7.1	7.2	7.5	7.1	7.1							7.2
Alcoholic beverages and tobacco	79.2	8.5	8.6	8.7	9.4	11.2	11.8							9.7
Clothing and footwear	56.9	-13.5	-14.3	-14.3	-14.2	-14.1	-14.1							-14.1
Housing, water, electricity, gas and other fuels	236.4	30.1	30.5	30.7	30.2	29.7	29.8							30.2
Furnishings, household equipment and routine maintenance of the house	67.9	-3.1	-3.3	-3.4	-3.4	-3.9	-3.9							-3.5
Health	14.3	16.5	17.0	17.4	17.9	20.3	20.7							18.3
Transport	101.4	5.8	5.8	6.8	6.8	8.2	7.6							6.8
Communications	22.5	24.2	23.1	23.0	22.9	21.5	21.4							22.7
Recreation and culture	95.5	7.4	8.7	7.6	7.0	7.5	9.1							7.9
Education	4.5	12.2	12.6	12.5	12.5	12.9	12.8							12.6
Hotels, cafés and restaurants	74.2	11.8	12.0	12.4	12.6	17.1	17.5							13.9
Miscellaneous goods and services	49.5	17.4	18.3	18.8	18.7	19.9	20.3							18.9

Source: CZSO

CONSUMER PRICES - TRADABLES AND NONTRADABLES

percentage changes; December 1999 = 100

Group	Constant 1999 weights in per mille	2000	2001	2002	2003			2004	
		12	12	12	6	9	12	3	6
1. Food and non-alcoholic beverages	197.6	4.6	7.9	2.1	4.2	1.1	5.7	7.2	7.1
- tradables	197.6	4.6	7.9	2.1	4.2	1.1	5.7	7.2	7.1
2. Alcoholic beverages and tobacco	79.2	2.4	5.4	7.1	7.6	7.9	7.8	8.7	11.8
- tradables	79.2	2.4	5.4	7.1	7.6	7.9	7.8	8.7	11.8
3. Clothing and footwear	56.9	-2.7	-3.9	-7.7	-10.4	-12.4	-11.9	-14.3	-14.1
- nontradables	1.4	6.1	13.0	18.3	20.0	20.9	21.1	25.6	34.4
- tradables	55.5	-2.9	-4.3	-8.4	-11.2	-13.2	-12.7	-15.3	-15.3
4. Housing, water, electricity, gas and other fuels	236.4	7.8	19.0	24.3	26.6	27.0	26.6	30.7	29.8
- nontradables	226.1	8.1	19.7	25.2	27.6	28.0	27.5	31.6	30.8
- tradables	10.3	2.3	2.7	4.0	4.0	4.5	5.9	10.9	8.5
5. Furnishings, household equipment and routine maintenance of the house	67.9	-0.7	-0.4	-1.0	-2.1	-2.7	-3.0	-3.4	-3.9
- nontradables	2.9	4.3	7.5	9.9	11.2	11.8	12.3	14.0	16.2
- tradables	65.0	-0.9	-0.8	-1.5	-2.7	-3.4	-3.7	-4.2	-4.8
6. Health	14.3	4.1	8.4	12.8	16.4	17.5	16.4	17.4	20.7
- nontradables	11.0	4.9	10.1	15.4	19.9	21.2	19.9	21.1	25.3
- tradables	3.3	1.5	2.7	4.4	5.1	5.4	5.1	5.3	5.7
7. Transport	101.4	6.9	3.4	4.1	3.8	4.3	3.6	6.8	7.6
- nontradables	27.4	6.2	11.7	16.0	17.6	18.1	18.4	22.2	22.7
- tradables	74.0	7.2	0.3	-0.3	-1.3	-0.8	-1.9	1.1	2.0
8. Communications	22.5	1.5	5.7	8.2	7.4	7.3	7.2	23.0	21.4
- nontradables	21.0	2.7	8.5	12.4	12.0	12.0	12.1	17.8	16.6
- tradables	1.5	-16.4	-34.7	-52.1	-58.3	-59.8	-62.3	96.8	89.8
9. Recreation and culture	95.5	2.0	7.2	7.2	7.0	6.1	6.1	7.6	9.1
- nontradables	60.4	4.4	14.3	16.2	17.7	16.6	16.7	19.0	22.4
- tradables	35.1	-2.2	-5.0	-8.3	-11.4	-12.1	-12.1	-12.0	-13.7
10. Education	4.5	3.4	6.8	11.3	11.6	11.0	12.0	12.5	12.8
- nontradables	4.5	3.4	6.8	11.3	11.6	11.0	12.0	12.5	12.8
11. Hotels, cafés and restaurants	74.2	2.6	5.9	8.7	9.6	10.3	10.8	12.4	17.5
- nontradables	74.2	2.6	5.9	8.7	9.6	10.3	10.8	12.4	17.5
12. Miscellaneous goods and services	49.5	3.1	8.7	11.9	14.6	14.9	15.2	18.8	20.3
- nontradables	22.0	5.7	17.5	25.8	33.9	34.8	36.4	43.7	47.7
- tradables	27.5	1.1	1.7	0.8	-0.8	-1.0	-1.7	-1.1	-1.5
Household consumer prices, total	1000.0	4.1	8.4	9.0	9.9	9.3	10.1	12.4	13.1
Tradables	549.1	2.5	2.9	0.2	0.2	-1.2	0.3	1.6	1.9
- food	276.8	4.0	7.2	3.5	5.2	3.0	6.3	7.6	8.4
- others	272.3	1.0	-1.5	-3.2	-4.9	-5.5	-5.8	-4.5	-4.8
Nontradables	450.9	6.0	15.2	19.7	21.8	22.1	22.0	25.5	26.7
- others	271.2	4.7	11.5	16.4	18.6	19.0	19.4	22.7	25.7
- regulated	179.7	8.0	20.6	24.6	26.7	26.8	26.0	29.8	28.3

CNB calculation based on CZSO data

INFLATION EXPECTATIONS OF SELECTED ECONOMIC SECTORS FOR 12 MONTHS AHEAD

annual percentage changes

	CPI		
	Financial market	Businesses	Households
1/00	4.0		
2/00	4.5		
3/00	4.5	4.3	4.1
4/00	4.2		
5/00	4.1		
6/00	4.4	4.8	4.1
7/00	4.6		
8/00	4.5		
9/00	4.7	5.0	4.6
10/00	4.6		
11/00	4.8		
12/00	5.0	4.7	4.1
1/01	4.5		
2/01	4.3		
3/01	4.2	4.2	4.0
4/01	4.0		
5/01	4.3		
6/01	4.6	4.8	5.1
7/01	4.6		
8/01	4.7		
9/01	4.8	4.7	4.9
10/01	4.4		
11/01	4.0		
12/01	3.9	3.9	4.6
1/02	3.8		
2/02	3.5		
3/02	3.5	3.6	3.9
4/02	3.5		
5/02	3.3		
6/02	3.1	2.7	1.6
7/02	2.8		
8/02	2.7		
9/02	3.1	2.4	1.3
10/02	2.5		
11/02	2.4		
12/02	2.3	2.3	2.3
1/03	2.5		
2/03	2.4		
3/03	2.5	2.1	4.3
4/03	2.6		
5/03	3.7		
6/03	3.2	2.6	1.7
7/03	3.3		
8/03	3.2		
9/03	3.1	2.6	3.1
10/03	3.0		
11/03	3.1		
12/03	3.3	2.9	4.2
1/04	2.9		
2/04	3.2		
3/04	3.0	3.3	4.9
4/04	2.8		
5/04	2.6		
6/04	2.7	3.1	4.9

Source: CNB statistical survey

HARMONISED INDEX OF CONSUMER PRICES

annual percentage changes

	2000	2001	2002	2003	2004
	12	12	12	12	6
Belgium	3.0	2.0	1.3	1.7	2.0
Denmark	2.3	2.1	2.6	1.2	0.9
Finland	2.9	2.3	1.7	1.2	-0.1
France	1.7	1.4	2.2	2.4	2.7
Ireland	4.6	4.4	4.6	2.9	2.5
Italy	2.8	2.2	3.0	2.5	2.4
Luxembourg	4.3	0.9	2.8	2.4	3.8
Germany	2.1	1.4	1.1	1.1	1.9
Netherlands	2.9	5.1	3.2	1.6	1.5
Portugal	3.8	3.9	4.0	2.3	3.7
Austria	1.8	1.8	1.7	1.3	2.3
Greece	3.7	3.5	3.5	3.1	3.0
Spain	4.0	2.5	4.0	2.7	3.5
Sweden	1.3	3.2	1.7	1.8	1.2
United Kingdom	0.9	1.0	1.7	1.3	1.6
European Union	2.2	1.9	2.2	1.8	2.2
Czech Republic	4.0	3.9	0.1	1.0	2.7

Source: Eurostat

MONETARY SURVEY

position at month-end in CZK billions

	2000	2001	2002	2003	2004
	12	12	12	12	5
Total assets	1412.3	1596.0	1651.8	1766.1	1809.7
Net external assets (NEAs)	673.1	800.6	926.1	822.0	906.1
NEAs of CNB			715.6	687.5	685.9
NEAs of OMFIs			210.5	134.5	220.2
Net domestic assets	739.2	795.4	725.8	944.1	903.6
Domestic loans	1068.8	1011.9	940.0	1145.5	1161.1
Net credit to government (NCG) (including securities)			215.8	354.0	345.4
NCG to central government (including securities)			260.4	408.7	411.3
NCG to other government (including securities)			-44.6	-54.8	-66.0
Loans to corporations and households (excluding securities)	963.9	775.4	724.2	791.6	815.8
Loans to corporations (excluding securities)	841.0	636.1	542.7	554.1	556.7
Loans to households (excluding securities)	122.9	139.3	181.5	237.5	259.1
Other net items (including securities and capital)	-329.6	-216.5	-214.3	-201.4	-257.5
Capital and reserves			-462.8	-398.5	-413.4
Holdings of securities			18.5	16.6	29.3
Issued securities			-48.6	-52.1	-85.3
Others			278.5	232.5	211.9
Liabilities					
Monetary aggregate M2	1412.3	1596.0	1651.8	1766.1	1809.7
Monetary aggregate M1	497.7	583.6	787.7	902.8	939.3
Currency in circulation	171.8	180.4	197.8	221.4	229.0
Overnight deposits			589.9	681.4	710.3
Overnight deposits - households			315.6	372.1	406.0
Overnight deposits - corporations			274.3	309.3	304.3
M2-M1 (quasi money)	914.6	1012.4	864.1	863.3	870.4
Deposits with agreed maturity			651.2	666.4	677.9
Deposits with agreed maturity - households			448.6	439.8	454.4
Deposits with agreed maturity - corporations			202.5	226.6	223.5
Deposits redeemable at notice			194.3	185.6	180.0
Deposits redeemable at notice - households			190.7	182.3	176.9
Deposits redeemable at notice - corporations			3.6	3.2	3.1
Repurchase agreements			18.6	11.3	12.5
Annual percentage changes					
M1	11.1	17.3	35.0	14.6	17.1
M2	5.6	13.0	3.5	6.9	9.0
Loans to corporations and households	-3.7	-19.6	-6.6	9.3	12.3
M2-M1 (deposits)	2.8	10.7	-14.6	-0.1	1.3
Annual percentage growth rates					
M1				15.5	18.1
M2				8.1	9.5
Loans to corporations and households				11.8	13.9
M2-M1 (deposits)				1.2	1.5

INTEREST RATES ON INTERBANK DEPOSITS

percentages

	2000	2001	2002	2003	2004
	12	12	12	12	6
1. AVERAGE PRIBOR 1)					
- 1 day	5.23	4.63	2.75	1.98	2.05
- 7 day	5.29	4.79	2.76	2.02	2.07
- 14 day	5.29	4.78	2.76	2.03	2.08
- 1 month	5.32	4.77	2.73	2.04	2.12
- 2 month	5.36	4.72	2.67	2.06	2.22
- 3 month	5.42	4.69	2.63	2.08	2.33
- 6 month	5.60	4.62	2.60	2.13	2.49
- 9 month	5.78	4.61	2.60	2.22	2.64
- 12 month	5.90	4.62	2.60	2.30	2.76
2. AVERAGE PRIBID 1)					
- 1 day	5.11	4.53	2.65	1.88	1.95
- 7 day	5.18	4.69	2.67	1.92	1.97
- 14 day	5.19	4.69	2.67	1.93	1.98
- 1 month	5.22	4.68	2.64	1.94	2.02
- 2 month	5.26	4.62	2.57	1.96	2.12
- 3 month	5.31	4.59	2.54	1.98	2.23
- 6 month	5.49	4.52	2.51	2.03	2.39
- 9 month	5.67	4.52	2.51	2.12	2.54
- 12 month	5.79	4.52	2.51	2.20	2.66

1) Commercial banks quoting their rates daily on the interbank deposit market

FRA RATES

percentages; monthly averages

	2000	2001	2002	2003	2004
	12	12	12	12	6
3 * 6	5.68	4.49	2.52	2.23	2.62
3 * 9	5.85	4.53	2.54	2.36	2.78
6 * 9	5.93	4.53	2.52	2.47	2.91
6 * 12	6.10	4.52	2.58	2.64	3.07
9 * 12	6.19	4.54	2.61	2.77	3.20
12 * 24	.	.			
9*12 - 3*6 spread	0.51	0.05	0.10	0.55	0.58
6*12 - 3*9 spread	0.25	-0.02	0.04	0.28	0.29

IRS RATES

percentages; monthly averages

	2000	2001	2002	2003	2004
	12	12	12	12	6
1Y	5.94	4.64	2.63	2.41	2.81
2Y	6.40	4.72	2.85	2.98	3.37
3Y	6.72	4.89	3.18	3.38	3.75
4Y	6.96	5.05	3.46	3.69	4.04
5Y	7.15	5.19	3.70	3.93	4.26
6Y	7.29	5.32	3.91	4.13	4.44
7Y	7.38	5.43	4.08	4.29	4.59
8Y	7.42	5.52	4.23	4.43	4.72
9Y	7.43	5.60	4.36	4.54	4.82
10Y	7.43	5.66	4.47	4.64	4.91
15Y	.	5.85	4.77	4.97	5.23
5Y - 1Y spread	1.21	0.56	1.07	1.52	1.45
10Y - 1Y spread	1.49	1.02	1.84	2.23	2.11

NOMINAL AND REAL INTEREST RATES (ex post approach)

percentages

	Nominal rates				Real rates based on CPI				Real rates based on PPI		
	PRIBOR		client rates		PRIBOR		client rates		PRIBOR		new client
	2W	1Y	new credits	time deposits	2W	1Y	new credits	time deposits	2W	1Y	credits
1/00	5.3	5.9	7.3	4.6	1.9	2.4	3.8	1.2	1.1	1.7	3.0
2/00	5.3	6.0	7.0	4.5	1.5	2.2	3.2	0.7	0.8	1.4	2.4
3/00	5.3	5.7	7.1	4.5	1.4	1.8	3.2	0.6	0.2	0.6	1.9
4/00	5.3	5.5	7.1	4.4	1.8	2.1	3.6	1.0	1.1	1.3	2.8
5/00	5.3	5.5	7.1	4.3	1.5	1.8	3.2	0.6	0.9	1.1	2.5
6/00	5.3	5.7	6.8	4.2	1.1	1.5	2.6	0.1	0.2	0.6	1.6
7/00	5.3	5.8	6.5	4.2	1.3	1.8	2.5	0.3	0.3	0.7	1.5
8/00	5.3	5.7	6.7	4.2	1.1	1.6	2.5	0.1	0.5	0.9	1.8
9/00	5.3	5.7	6.8	4.2	1.1	1.6	2.6	0.1	-0.1	0.3	1.4
10/00	5.3	5.8	6.6	4.0	0.9	1.3	2.1	-0.3	-0.6	-0.1	0.7
11/00	5.3	5.9	6.7	4.0	1.0	1.5	2.3	-0.3	-0.6	0.0	0.7
12/00	5.3	5.9	6.8	3.9	1.2	1.8	2.7	-0.1	0.3	0.9	1.7
1/01	5.3	5.6	6.3	3.9	1.0	1.3	2.0	-0.3	1.0	1.3	2.0
2/01	5.2	5.3	6.2	3.9	1.2	1.3	2.1	-0.1	0.5	0.6	1.4
3/01	5.0	5.1	6.2	3.7	0.9	0.9	2.0	-0.3	0.9	0.9	2.0
4/01	5.0	5.0	6.2	3.7	0.4	0.4	1.5	-0.9	1.0	0.9	2.1
5/01	5.0	5.0	6.3	3.7	0.0	0.0	1.2	-1.2	1.2	1.2	2.4
6/01	5.0	5.3	6.3	3.7	-0.4	-0.2	0.7	-1.7	1.6	1.8	2.8
7/01	5.1	5.6	6.4	3.7	-0.8	-0.2	0.5	-2.1	2.0	2.6	3.3
8/01	5.3	6.0	6.6	3.7	-0.2	0.5	1.0	-1.7	2.8	3.5	4.1
9/01	5.3	5.7	6.6	3.7	0.6	0.9	1.8	-0.9	3.4	3.8	4.7
10/01	5.3	5.3	6.6	3.7	0.9	0.9	2.1	-0.7	3.9	4.0	5.3
11/01	5.2	4.9	6.3	3.6	1.0	0.7	2.0	-0.5	4.3	4.0	5.4
12/01	4.8	4.6	5.9	3.3	0.7	0.5	1.7	-0.8	4.0	3.8	5.1
1/02	4.7	4.5	5.7	3.2	1.0	0.8	2.0	-0.4	4.1	3.9	5.1
2/02	4.3	4.4	5.1	3.0	0.4	0.5	1.1	-0.8	4.4	4.5	5.2
3/02	4.3	4.5	5.3	3.0	0.6	0.8	1.6	-0.7	4.5	4.7	5.5
4/02	4.2	4.4	5.1	2.9	1.0	1.1	1.8	-0.2	4.3	4.5	5.2
5/02	3.8	4.1	4.9	2.8	1.3	1.5	2.3	0.3	4.3	4.6	5.4
6/02	3.8	3.9	5.0	2.9	2.6	2.7	3.8	1.7	4.6	4.8	5.9
7/02	3.5	3.4	4.5	2.8	2.9	2.8	3.9	2.2	4.7	4.6	5.7
8/02	3.0	3.1	4.4	2.3	2.4	2.5	3.8	1.7	4.0	4.1	5.4
9/02	3.0	3.0	4.5	2.5	2.2	2.1	3.7	1.7	4.0	3.9	5.5
10/02	3.0	2.8	4.6	2.3	2.4	2.2	4.0	1.7	3.9	3.7	5.5
11/02	2.8	2.8	4.2	2.1	2.3	2.2	3.7	1.6	3.5	3.5	4.9
12/02	2.8	2.6	4.2	2.2	2.1	2.0	3.6	1.6	3.5	3.3	4.9
1/03	2.7	2.6	4.1	2.2	3.2	3.0	4.5	2.6	3.6	3.5	5.0
2/03	2.5	2.4	3.9	2.1	2.9	2.8	4.3	2.5	3.2	3.2	4.6
3/03	2.5	2.4	3.9	2.0	2.9	2.8	4.3	2.5	2.9	2.8	4.3
4/03	2.5	2.4	3.9	2.0	2.6	2.5	4.0	2.1	3.2	3.2	4.7
5/03	2.5	2.4	4.0	2.0	2.5	2.4	4.0	2.0	3.3	3.3	4.8
6/03	2.5	2.3	3.8	1.9	2.2	2.0	3.5	1.6	3.4	3.2	4.8
7/03	2.3	2.2	3.5	1.7	2.4	2.3	3.6	1.8	2.9	2.9	4.2
8/03	2.0	2.1	3.3	1.8	2.1	2.2	3.4	1.9	2.4	2.5	3.7
9/03	2.0	2.2	3.6	1.7	2.0	2.2	3.6	1.7	2.0	2.2	3.6
10/03	2.0	2.2	3.7	1.7	1.6	1.8	3.3	1.3	2.1	2.3	3.8
11/03	2.0	2.2	3.5	1.8	1.0	1.2	2.5	0.7	1.6	1.8	3.1
12/03	2.0	2.3	3.7	1.7	1.0	1.3	2.6	0.7	1.1	1.4	2.7
1/04	2.0	2.3	5.5	1.4	-0.3	0.0	3.1	-0.9	0.4	0.7	3.9
2/04	2.0	2.3	5.0	1.4	-0.3	0.0	2.7	-0.9	0.5	0.8	3.5
3/04	2.0	2.3	5.1	1.6	-0.5	-0.2	2.6	-0.9	-0.1	0.2	3.0
4/04	2.0	2.3	5.4	1.5	-0.3	0.0	3.0	-0.8	-1.6	-1.4	1.6
5/04	2.0	2.5	5.4	1.4	-0.7	-0.2	2.6	-1.2	-2.7	-2.3	0.5
6/04	2.1	2.8			-0.8	-0.1			-3.9	-3.2	

Note: real rates = nominal rates deflated by annual index (CPI/PPI) in given month
Starting from January 2004, methodology for new credits and time deposits was changed. Newly drawn credits were replaced by newly granted credits.

REAL INTEREST RATES (ex ante approach)

percentages

	Real rates expected by financial markets				Real rates expected by businesses				Real rates expected by households			
	PRIBOR		client rates		PRIBOR		client rates		PRIBOR		client rates	
	2W	1Y	new credits	time deposits	2W	1Y	new credits	time deposits	2W	1Y	new credits	time deposits
1/00	1.3	1.8	3.2	0.6								
2/00	0.8	1.4	2.4	0.0								
3/00	0.8	1.2	2.5	0.0	1.0	1.3	2.7	0.2	1.1	1.5	2.9	0.4
4/00	1.1	1.3	2.8	0.2								
5/00	1.1	1.4	2.8	0.2								
6/00	0.9	1.2	2.3	-0.1	0.5	0.9	1.9	-0.5	1.1	1.5	2.6	0.1
7/00	0.7	1.1	1.9	-0.4								
8/00	0.8	1.2	2.1	-0.3								
9/00	0.6	1.0	2.0	-0.5	0.3	0.7	1.8	-0.8	0.7	1.1	2.1	-0.4
10/00	0.7	1.1	1.9	-0.5								
11/00	0.5	1.0	1.8	-0.8								
12/00	0.3	0.9	1.7	-1.1	0.6	1.1	2.0	-0.8	1.1	1.7	2.6	-0.2
1/01	0.8	1.1	1.8	-0.6								
2/01	0.9	1.0	1.8	-0.4								
3/01	0.8	0.8	1.9	-0.4	0.8	0.8	1.9	-0.4	1.0	1.0	2.1	-0.3
4/01	1.0	0.9	2.1	-0.3								
5/01	0.7	0.7	1.9	-0.6								
6/01	0.4	0.7	1.6	-0.8	0.2	0.5	1.4	-1.0	-0.1	0.2	1.1	-1.3
7/01	0.5	1.0	1.7	-0.8								
8/01	0.6	1.2	1.8	-0.9								
9/01	0.5	0.8	1.7	-1.0	0.5	0.8	1.7	-1.0	0.4	0.7	1.6	-1.1
10/01	0.9	0.9	2.1	-0.7								
11/01	1.2	0.9	2.2	-0.4								
12/01	0.9	0.7	1.9	-0.6	0.9	0.7	1.9	-0.6	0.2	0.0	1.2	-1.2
1/02	0.9	0.7	1.9	-0.5								
2/02	0.8	0.8	1.5	-0.4								
3/02	0.8	1.0	1.8	-0.5	0.7	0.9	1.7	-0.6	0.4	0.6	1.4	-0.9
4/02	0.7	0.8	1.5	-0.5								
5/02	0.5	0.7	1.5	-0.5								
6/02	0.7	0.8	1.9	-0.2	1.1	1.2	2.3	0.2	2.2	2.3	3.4	1.3
7/02	0.7	0.6	1.7	0.0								
8/02	0.3	0.4	1.7	-0.4								
9/02	-0.1	-0.1	1.4	-0.6	1.1	1.0	2.6	0.6	1.7	1.6	3.2	1.2
10/02	0.5	0.3	2.0	-0.2								
11/02	0.4	0.3	1.8	-0.3								
12/02	0.5	0.3	1.9	-0.1	0.5	0.3	1.9	-0.1	0.5	0.3	1.9	-0.1
1/03	0.2	0.1	1.6	-0.3								
2/03	0.1	0.0	1.4	-0.3								
3/03	0.0	-0.1	1.3	-0.4	0.4	0.3	1.7	-0.1	-1.7	-1.9	-0.4	-2.2
4/03	-0.1	-0.2	1.3	-0.6								
5/03	-1.2	-1.2	0.3	-1.6								
6/03	-0.7	-0.9	0.6	-1.2	-0.1	-0.3	1.2	-0.6	0.8	0.6	2.1	0.2
7/03	-1.0	-1.0	0.2	-1.5								
8/03	-1.1	-1.1	0.1	-1.4								
9/03	-1.0	-0.9	0.5	-1.3	-0.6	-0.4	1.0	-0.8	-1.0	-0.9	0.5	-1.3
10/03	-0.9	-0.8	0.6	-1.2								
11/03	-1.0	-0.8	0.4	-1.3								
12/03	-1.2	-1.0	0.4	-1.5	-0.8	-0.6	0.7	-1.1	-2.1	-1.8	-0.5	-2.4
1/04	-0.9	-0.6	2.5	-1.4								
2/04	-1.2	-0.8	1.8	-1.7								
3/04	-1.0	-0.7	2.1	-1.4	-1.2	-1.0	1.8	-1.7	-2.8	-2.5	0.2	-3.2
4/04	-0.8	-0.5	2.5	-1.3								
5/04	-0.6	-0.1	2.7	-1.1								
6/04	-0.6	0.1			-1.0	-0.3			-2.7	-2.0		

Note: real rates = nominal rates deflated by inflation expected by selected economic sectors according to the CNB statistical survey
Starting from January 2004, methodology for new credits and time deposits was changed. Newly drawn credits were replaced by newly granted credits.

KORUNA INTEREST RATES (stock of business)

percentages

	2000	2001	2002	2003	2004
	12	12	12	12	5
Koruna interest rates on loans provided by banks to residents:					
Households and non-profit institutions serving households (S.14+S.15) - total		8.74	8.77	8.24	8.11
- maturity up to 1 year		8.20	10.35	11.21	12.27
- maturity over 1 year and up to 5 years		10.55	10.80	10.17	11.90
- maturity over 5 years		8.02	7.35	6.65	6.49
- for consumption - total			13.83	13.83	15.01
- maturity up to 1 year			13.05	14.26	15.58
- maturity over 1 year and up to 5 years			14.48	13.86	15.18
- maturity over 5 years			12.55	13.21	13.60
- for house purchase - total			7.11	6.31	6.17
- maturity up to 1 year			7.67	6.24	5.19
- maturity over 1 year and up to 5 years			7.90	7.05	7.06
- maturity over 5 years			6.88	6.09	6.08
- other - total			6.99	7.80	7.22
- maturity up to 1 year			6.64	8.49	7.90
- maturity over 1 year and up to 5 years			6.34	8.02	7.55
- maturity over 5 years			7.61	7.02	6.69
Non-financial corporations (S.11) - total		6.84	5.19	4.53	4.31
- maturity up to 1 year		6.32	4.34	4.08	3.75
- maturity over 1 year and up to 5 years		6.93	5.47	4.64	4.33
- maturity over 5 years		7.52	6.34	5.14	5.18
Koruna interest rates on deposits accepted by banks from residents:					
Households and non-profit institutions serving households (S.14+S.15) - total		2.63	1.72	1.30	1.30
- overnight		1.42	0.94	0.50	0.50
- with agreed maturity - total		3.11	2.26	2.02	2.03
- with agreed maturity up to 2 years			1.68	0.96	0.98
- with agreed maturity over 2 years			3.04	2.90	2.81
- redeemable at notice - total			1.81	1.26	1.33
- redeemable at notice up to 3 months			1.93	1.67	1.75
- redeemable at notice over 3 months			1.73	0.98	1.01
- repurchase agreements					
Non-financial corporations (S.11) - total		1.96	1.25	0.85	1.05
- overnight		1.00	0.94	0.64	0.65
- with agreed maturity - total		3.62	2.16	1.50	1.63
- with agreed maturity up to 2 years			2.15	1.49	1.60
- with agreed maturity over 2 years			3.47	3.04	2.85
- redeemable at notice - total			1.64	1.17	1.13
- redeemable at notice up to 3 months			1.60	1.14	1.08
- redeemable at notice over 3 months			2.26	1.32	1.49
- repurchase agreements			2.42	0.75	1.77

BALANCE OF PAYMENTS 1)

in CZK millions

	2000	2001	2002	2003	2004 2)
	Q1 - 4	Q1 - 4	Q1 - 4	Q1 - 4	Q1
A. Current account	**-104 877.1**	**-124 478.3**	**-136 378.1**	**-157 217.9**	**-16 741.1**
Balance of trade 3)	-120 825.0	-116 685.0	-71 323.0	-69 392.0	-923.0
exports	1 121 099.0	1 269 634.0	1 254 394.0	1 371 810.0	374 667.0
imports	1 241 924.0	1 386 319.0	1 325 717.0	1 441 202.0	375 590.0
Services	54 559.8	57 984.9	21 850.8	13 236.7	1 803.1
credit	264 806.2	269 689.6	231 131.1	219 151.1	52 835.1
transport	53 734.3	57 492.3	56 560.5	60 556.3	15 873.3
travel	115 071.0	118 133.0	96 289.2	100 310.1	22 630.3
others	96 000.9	94 064.3	78 281.4	58 284.7	14 331.5
debit	210 246.4	211 704.7	209 280.3	205 914.4	51 032.0
transport	27 543.0	30 570.5	29 332.8	33 725.7	9 204.8
travel	49 370.0	52 802.0	51 549.3	54 419.2	11 600.0
others	133 333.4	128 332.2	128 398.2	117 769.5	30 227.2
Income	-52 978.4	-83 548.9	-115 615.0	-116 644.7	-19 200.8
credit	75 439.1	84 892.3	66 790.1	74 410.3	19 136.5
debit	128 417.5	168 441.2	182 405.1	191 055.0	38 337.3
Current transfers	14 366.5	17 770.7	28 709.1	15 582.1	1 579.6
credit	36 594.6	36 404.9	46 709.0	46 773.7	7 011.2
debit	22 228.1	18 634.2	17 999.9	31 191.6	5 431.6
B. Capital account	**-198.2**	**-330.7**	**-119.4**	**-82.2**	**-22.2**
credit	223.4	90.4	221.0	198.2	135.0
debit	421.6	421.1	340.4	280.4	157.2
Total A + B	*-105 075.3*	*-124 809.0*	*-136 497.5*	*-157 300.1*	*-16 763.3*
C. Financial account	**148 046.6**	**172 849.9**	**347 827.4**	**163 854.2**	**3 561.9**
Direct investment	190 767.4	208 296.1	270 930.2	66 353.0	30 074.9
abroad	-1 653.7	-6 289.2	-6 759.3	-6 546.5	-1 396.6
equity capital and reinvested earnings	-1 245.9	-5 848.5	-5 376.8	-324.1	-1 361.2
other capital	-407.8	-440.7	-1 382.5	-6 222.4	-35.4
in the Czech Republic	192 421.1	214 585.3	277 689.5	72 899.5	31 471.5
equity capital and reinvested earnings	171 777.2	185 981.4	270 061.0	66 811.9	28 787.8
other capital	20 643.9	28 603.9	7 628.5	6 087.6	2 683.7
Portfolio investment	-68 172.9	34 857.3	-46 748.7	-37 715.0	25 613.4
assets	-86 631.8	4 405.6	-75 602.1	-85 888.6	3 567.8
equity securities	-44 181.0	9 447.8	-7 807.9	5 630.5	-8 095.7
debt securities	-42 450.8	-5 042.2	-67 794.2	-91 519.1	11 663.5
liabilities	18 458.9	30 451.7	28 853.4	48 173.6	22 045.6
equity securities	23 810.9	23 203.6	-9 035.7	30 133.5	12 146.6
debt securities	-5 352.0	7 248.1	37 889.1	18 040.1	9 899.0
Financial derivatives	-1 402.8	-3 220.3	-4 281.7	3 860.1	-311.5
assets	-4 501.6	-9 407.6	-15 458.4	7 083.7	-764.2
liabilities	3 098.8	6 187.3	11 176.7	-3 223.6	452.7
Other investment	26 854.9	-67 083.2	127 927.6	131 356.1	-51 814.9
assets	35 832.1	-46 144.5	133 121.8	67 045.4	-793.9
long-term	21 322.2	1 325.8	28 711.4	1 115.4	2 509.2
CNB					
commercial banks	14 362.2	-4 125.8	5 271.7	-999.9	2 560.0
government	2 937.0	6 928.9	25 333.6	5 688.4	1 072.7
other sectors	4 023.0	-1 477.3	-1 893.9	-3 573.1	-1 123.5
short-term	14 509.9	-47 470.3	104 410.4	65 930.0	-3 303.1
commercial banks	22 001.9	-45 523.2	122 163.8	44 971.2	21 642.6
government		-87.1	-2 237.4	2 193.8	-1 339.7
other sectors	-7 492.0	-1 860.0	-15 516.0	18 765.0	-23 606.0
liabilities	-8 977.2	-20 938.7	-5 194.2	64 310.7	-51 021.0
long-term	-26 212.5	-4 262.6	2 853.8	21 349.6	2 038.1
CNB	-22.8	-22.0	-20.2	-20.4	-10.4
commercial banks	-31 523.7	-7 222.2	-8 059.2	-1 663.8	1 112.8
government	-1 837.6	-5 000.8	-1 517.2	10 304.7	2 125.2
other sectors	7 171.6	7 982.4	12 450.4	12 729.1	-1 189.5
short-term	17 235.3	-16 676.1	-8 048.0	42 961.1	-53 059.1
CNB	-17.0	59.7	-24.3	-21.4	-8.6
commercial banks	-3 812.5	-35 688.6	-3 871.2	37 899.4	-66 690.8
government					
other sectors	21 064.8	18 952.8	-4 152.5	5 083.1	13 640.3
Total A + B + C	*42 971.3*	*48 040.9*	*211 329.9*	*6 554.1*	*-13 201.4*
D. Net errors and omissions. valuation changes	**-11 378.5**	**19 112.1**	**5 615.1**	**6 349.3**	**20 060.0**
Total A + B + C + D	*31 592.8*	*67 153.0*	*216 945.0*	*12 903.4*	*6 858.6*
E. Change in reserves (- increase)	**-31 592.8**	**-67 153.0**	**-216 945.0**	**-12 903.4**	**-6 858.6**

1) Balance of payments structure based on the Balance of Payments Manual (5th edition), IMF 1993
2) Preliminary data
3) In accordance with customs statistics methodology in force since 1 July 2000

INTERNATIONAL INVESTMENT POSITION

in CZK millions

	2000	2001	2002	2003	2004
	31 Dec.	31 Dec.	31 Dec.	31 Dec.	31 Mar. 1)
ASSETS	1 448 400.7	1 544 963.0	1 579 922.9	1 527 647.8	1 568 898.9
Direct investment abroad	27 899.3	41 176.1	44 397.1	49 040.0	52 085.0
- equity capital	24 797.5	37 633.6	39 472.1	38 005.0	40 735.0
- other capital	3 101.8	3 542.5	4 925.0	11 035.0	11 350.0
Portfolio investment	180 431.3	185 138.6	274 344.7	343 854.4	340 623.4
- equity securities	92 222.9	68 675.5	86 464.7	47 337.7	55 339.3
- debt securities	88 208.4	116 463.1	187 880.0	296 516.7	285 284.1
Financial derivatives	6 347.2	15 754.8	31 213.2	24 129.5	24 893.7
Other investment	736 903.7	778 435.7	515 356.2	419 109.0	426 417.8
Long-term	315 625.5	310 133.9	179 639.6	157 598.6	159 606.8
- CNB	329.1	307.3	280.9	468.4	488.6
- commercial banks	75 537.9	79 663.7	67 966.9	66 121.3	64 756.5
- government	220 777.8	210 694.9	97 156.8	79 483.9	81 376.7
- other sectors	18 980.7	19 468.0	14 235.0	11 525.0	12 985.0
Short-term	421 278.2	468 301.8	335 716.6	261 510.4	266 811.0
- CNB	52.9	51.2	376.7	98.8	74.5
- commercial banks	314 115.3	359 638.5	213 815.4	161 140.9	142 154.4
of which: gold and foreign exchange	228 961.7	257 138.6	163 032.9	115 875.5	82 953.3
- government		87.1	2 324.5	130.7	1 442.1
- other sectors	107 110.0	108 525.0	119 200.0	100 140.0	123 140.0
CNB reserves	496 819.2	524 457.8	714 611.7	691 514.9	724 879.0
- gold	4 640.4	4 469.9	4 653.8	4 784.3	4 974.2
- SDR	7.7	31.0	137.1	238.7	
- reserve position in the IMF	116.0	5 478.3	7 081.5	11 949.9	12 377.1
- foreign exchange	491 001.2	514 188.0	686 516.1	674 451.8	707 462.7
- other reserve assets	1 053.9	290.6	16 223.2	90.2	65.0
LIABILITIES	1 640 270.0	1 789 030.7	1 977 177.7	2 143 363.3	2 187 870.3
Direct investment in the Czech Republic	818 411.6	982 335.0	1 165 529.1	1 219 263.4	1 253 991.2
- equity capital	702 217.8	837 537.3	1 013 102.9	1 063 633.4	1 092 421.2
- other capital	116 193.8	144 797.7	152 426.2	155 630.0	161 570.0
Portfolio investment	164 592.0	180 346.2	201 120.0	248 782.8	300 263.0
- equity securities	115 670.6	128 740.1	128 097.7	165 951.0	209 311.2
- debt securities	48 921.4	51 606.1	73 022.3	82 831.8	90 951.8
Financial derivatives	5 307.9	11 495.2	22 671.9	19 448.3	19 901.0
Other investment	651 958.5	614 854.3	587 856.7	655 868.8	613 715.1
Long-term	352 323.4	332 593.2	326 321.3	355 276.9	362 256.1
- CNB	180.4	133.4	114.5	96.1	85.0
- commercial banks	84 607.4	73 688.6	63 541.0	61 454.0	63 337.1
- government	19 699.2	9 476.2	9 475.8	22 456.0	24 723.2
- other sectors	247 836.4	249 295.0	253 190.0	271 270.8	274 110.8
Short-term	299 635.1	282 261.1	261 535.4	300 591.9	251 459.0
- CNB	8.8	68.5	44.2	22.8	14.2
- commercial banks	226 176.2	190 487.6	176 196.2	208 534.1	144 894.8
- government					
- other sectors	73 450.1	91 705.0	85 295.0	92 035.0	106 550.0
NET INVESTMENT POSITION	-191 869.3	-244 067.7	-397 254.8	-615 715.5	-618 971.4

1) Preliminary data

EXTERNAL DEBT

in CZK millions

	2000	2001	2002	2003	2004
	31 Dec.	31 Dec.	31 Dec.	31 Dec.	31 Mar. 1)
DEBT IN CONVERTIBLE CURRENCIES	808 122.8	811 258.1	813 305.2	894 330.6	866 236.9
of which:					
Long-term	464 323.8	465 687.8	498 833.8	538 585.7	552 798.2
By debtor					
- CNB	180.4	133.4	114.5	96.1	85.0
- commercial banks	95 737.1	88 401.4	80 063.7	76 674.1	83 575.2
- government	29 753.5	30 839.2	47 701.3	69 029.9	71 185.6
- other sectors	338 652.8	346 313.8	370 954.3	392 785.6	397 952.4
By creditor					
- foreign banks	228 709.6	229 305.5	230 589.8	246 533.0	253 698.7
- government institutions	3 405.7	2 373.6	1 747.2		
- multilateral institutions	67 521.2	70 879.0	69 894.7	83 779.6	83 671.6
- suppliers and direct investors	99 560.2	105 944.3	118 829.4	116 880.0	120 420.0
- other investors	65 127.1	57 185.4	77 772.7	91 393.1	95 007.9
Short-term	343 799.0	345 570.3	314 471.4	355 744.9	313 438.7
By debtor					
- CNB	8.8	68.5	44.2	22.8	14.2
- commercial banks	226 246.1	192 438.4	177 474.4	210 017.1	146 173.0
- government	2 115.0	465.0	761.0	710.0	5 268.7
- other sectors	115 429.1	152 598.4	136 191.8	144 995.0	161 982.8
By creditor					
- foreign banks	203 333.8	192 126.4	168 200.7	219 391.2	157 939.2
- suppliers and direct investors	106 988.6	116 278.4	112 256.8	101 210.0	114 640.0
- other investors	33 476.6	37 165.5	34 013.9	35 143.7	40 859.5
DEBT IN NON-CONVERTIBLE CURRENCIES	8 950.9	0.0	0.0	0.0	0.0
of which:					
- long-term	8 950.9				
- short-term					
TOTAL EXTERNAL DEBT	817 073.7	811 258.1	813 305.2	894 330.6	866 236.9
of which:					
- long-term	473 274.7	465 687.8	498 833.8	538 585.7	552 798.2
- short-term	343 799.0	345 570.3	314 471.4	355 744.9	313 438.7

1) Preliminary data

EXCHANGE RATES

A. NOMINAL RATE

in CZK; foreign exchange market rates

	2000	2001	2002	2003	2004
	1-12	1-12	1-12	1-12	3-6
CZK EXCHANGE RATE AGAINST SELECTED CURRENCIES					
- annual/quarterly averages					
1 EUR	35.61	34.08	30.81	31.84	32.03
1 USD	38.59	38.04	32.74	28.23	26.59
100 SKK	83.64	78.68	72.22	76.75	79.92
	12	12	12	12	6
- monthly averages					
1 EUR	34.82	32.59	31.19	32.31	31.61
1 USD	38.94	36.48	30.65	26.32	26.05
100 SKK	80.07	75.61	74.67	78.57	79.18
	31 Dec.	31 Dec.	31 Dec.	31 Dec.	30 Jun.
- last day of the month					
1 EUR	35.09	31.98	31.60	32.41	31.76
1 USD	37.81	36.26	30.14	25.65	26.14
100 SKK	79.70	74.81	75.18	78.71	79.63

B. NOMINAL EFFECTIVE RATE

	2000	2001	2002	2003	2004
					6
CZK nominal effective exchange rate (percentages) (2000=100)					
weights - foreign trade turnover	100.0	104.3	116.5	116.0	117.0
weights - foreign trade turnover SITC 5-8	100.0	104.4	116.1	115.6	116.2

Drawing on CZSO statistics on the geographical and commodity structure of foreign trade for 2000, 23 countries which account for around 90% of the Czech Republic's foreign trade were selected. The weights were processed in two alternatives:
Alternative I, used by the IMF, applies to the Czech Republic's entire foreign trade turnover
Alternative II, used by the European Central Bank, applies to only four commodity groups of the Czech Republic's foreign trade

C. REAL EFFECTIVE RATE

	2000	2001	2002	2003	2004
					5
CZK real effective exchange rate (percentages) (2000=100)					
a) industrial producer prices					
weights - foreign trade turnover	100.0	104.0	114.9	111.2	111.5
weights - foreign trade turnover SITC 5-8	100.0	104.6	115.6	112.0	112.9
b) consumer prices					
weights - foreign trade turnover	100.0	105.5	116.7	112.6	111.7
weights - foreign trade turnover SITC 5-8	100.0	106.2	117.5	113.4	112.9

Source: CZSO - consumer prices and industrial producer prices of the Czech Republic
Monthly IMF publication - International Financial Statistics - and the CNB's own calculations

PUBLIC FINANCES

in CZK billions

	2000	2001	2002	2003	2004
	1-12	1-12	1-12	1-12	1-6
STATE BUDGET					
TOTAL REVENUE	586.2	626.2	705.0	699.7	366.6
Tax revenue	559.5	598.3	627.4	667.5	339.4
Taxes on income, profits and capital gains	87.0	147.4	159.0	172.9	91.8
Domestic taxes on goods and services	216.8	187.0	186.9	198.4	94.2
- value-added taxes	145.9	121.3	118.1	125.6	57.4
- excises	70.9	65.7	68.9	72.9	36.8
Taxes on international trade and transactions	13.6	10.0	9.8	10.2	4.3
Taxes on property	6.0	6.4	7.9	8.8	5.2
Social and health security contributions and payroll taxes	222.2	242.3	258.5	272.4	141.6
Non-tax and capital incomes and received subsidies	26.7	27.9	77.7	32.2	27.3
TOTAL EXPENDITURE	632.3	693.9	750.8	808.7	416.3
Current expenditure	571.4	642.5	697.3	745.4	399.1
Capital expenditure	60.9	51.4	53.5	63.3	17.3
Public budgets (balance in IMF GFS methodology)	-62.0	-52.3	-11.8	-134.2	
state budget	-46.1	-67.7	-45.7	-109.1	-49.7
local budget	-2.5	-11.2	-4.3	-5.5	
state financial assets	-5.7	.	.	.	
state funds	2.6	11.2	12.3	7.4	
Land Fund	-0.5	-0.1	-0.5	-0.7	
National Property Fund	-11.5	13.2	28.4	-27.0	
health insurance companies	2.1	1.4	-1.2	-0.3	
others	-0.4	0.9	-0.8	1.0	

CAPITAL MARKET

A. STOCK MARKET INDICES

last day of the month in points

	2000	2001	2002	2003	2004
	12	12	12	12	6
BCPP					
PX 50	478.5	394.6	460.7	659.1	793.5
PX-D	1366.0	1065.6	1166.4	1642.7	1994.8
PX-GLOB	570.6	492.9	576.8	816.9	981.2
RM-SYSTÉM					
PK-30	724.8	593.0	672.5	947.5	1097.8

B. TRADE VOLUMES

in CZK millions

	2000	2001	2002	2003	2004
	12	12	12	12	6
BCPP					
Monthly trade volumes	73 240.5	142 803.6	109 264.8	98 640.0	93 834.9
of which:					
a) shares	11 113.9	12 819.3	17 089.3	28 296.0	24 472.1
b) units	61.3	4.3	0.0	0.0	0.0
c) bonds	62 065.3	129 980.0	92 175.5	70 344.0	69 362.8
RM-SYSTÉM					
Monthly trade volumes	4 861.7	2 162.5	4 412.1	1 103.0	159.7
of which:					
a) shares	4 190.1	1 841.0	298.4	1 082.5	124.3
b) units	25.9	212.2	1.0	3.7	2.1
c) bonds	645.7	109.3	4 112.7	16.8	33.3

CNB MONETARY POLICY INSTRUMENTS

	2W repo rate (%)	Discount rate (%)	Lombard rate (%)	Minimum reserve requirement for primary deposits (%)	
				Banks	Building societies and ČMZRB
	1999				
18 January	8.75				
28 January				5.0	
29 January	8.00				
12 March	7.50	6.0	10.0		
9 April	7.20				
4 May	6.90				
25 June	6.50				
30 July	6.25				
3 September	6.00	5.5	8.0		
5 October	5.75				
7 October				**2.0**	**2.0**
27 October	5.50	5.0	7.5		
26 November	5.25				
	2000				
	No changes made				
	2001				
23 February	5.00	4.0	6.0		
27 July	5.25	4.25	6.25		
30 November	4.75	3.75	5.75		
	2002				
22 January	4.50	3.50	5.50		
1 February	4.25	3.25	5.25		
26 April	3.75	2.75	4.75		
26 July	3.00	2.00	4.00		
1 November	2.75	1.75	3.75		
	2003				
31 January	2.50	1.50	3.50		
26 June	2.25	1.25	3.25		
1 August	2.00	1.00	3.00		
	2004				
25 June	**2.25**	**1.25**	**3.25**		

MACROECONOMIC AGGREGATES

in CZK millions; annual percentage changes; constant 2000 prices

	2000	2001	2002	2003	2004
	Q1 - 4	Q1 - 4	Q1 - 4	Q1 - 4	Q1
GROSS DOMESTIC PRODUCT					
- in CZK millions	2 150 058	2 206 794	2 239 669	2 309 392	570 366
- percentages	3.9	2.6	1.5	3.1	3.1
FINAL CONSUMPTION					
- in CZK millions	1 597 796	1 645 430	1 699 986	1 769 417	421 804
- percentages	2.1	3.0	3.3	4.1	2.3
of which:					
Households					
- in CZK millions	1 108 838	1 140 035	1 171 297	1 229 033	296 886
- percentages	2.9	2.8	2.7	4.9	3.9
Government					
- in CZK millions	474 954	493 113	515 411	526 679	121 222
- percentages	0.2	3.8	4.5	2.2	-1.6
Non-profit institutions					
- in CZK millions	14 004	12 282	13 278	13 705	3 696
- percentages	-0.2	-12.3	8.1	3.2	4.9
GROSS CAPITAL FORMATION					
- in CZK millions	618 527	657 744	680 488	718 973	188 030
- percentages	9.1	6.3	3.5	5.7	12.7
of which:					
Fixed capital					
- in CZK millions	594 913	627 019	648 431	696 156	169 488
- percentages	4.9	5.4	3.4	7.4	9.5
Changes in inventories					
- in CZK millions	23 321	30 560	31 838	22 616	18 494
Acquisitions less disposals of valuables					
- in CZK millions	293	165	219	201	48
- percentages	144.2	-43.7	32.7	-8.2	-14.3
TRADE BALANCE					
- in CZK millions	-66 265	-96 380	-141 636	-183 800	-39 079
of which:					
Exports of goods					
- in CZK millions	1 121 099	1 283 020	1 359 710	1 466 864	388 595
- percentages	19.6	14.4	6.0	7.9	8.2
Exports of services					
- in CZK millions	264 806	261 756	220 189	207 006	49 625
- percentages	4.8	-1.2	-15.9	-6.0	9.3
Imports of goods					
- in CZK millions	1 241 924	1 424 031	1 490 075	1 630 755	421 712
- percentages	20.0	14.7	4.6	9.4	11.2
Imports of services					
- in CZK millions	210 246	217 125	231 460	226 915	55 587
- percentages	-1.6	3.3	6.6	-2.0	12.2
FINAL DOMESTIC DEMAND					
- in CZK millions	2 192 709	2 272 449	2 348 417	2 465 573	591 292
- percentages		3.6	3.3	5.0	4.2
AGGREGATE DOMESTIC DEMAND					
- in CZK millions	2 216 323	2 303 174	2 380 474	2 488 390	609 834
- percentages		3.9	3.4	4.5	5.3
GROSS DOMESTIC PRODUCT AT CURRENT PRICES					
- in CZK millions	2 150 058	2 315 255	2 414 669	2 532 388	637 921
- percentages	5.3	7.7	4.3	4.9	7.3

Source: CZSO

LABOUR MARKET

A. NATIONAL ACCOUNTS FOR THE HOUSEHOLD SECTOR

annual percentage changes

	2000	2001	2002	2003	2004
	Q1 - 4	Q1 - 4	Q1 - 4	Q1 - 4	Q1
Current income	5.0	5.7	6.4	4.3	5.9
of which:					
- gross operating surplus and mixed income	7.2	8.3	2.4	4.0	2.8
- compensation of employees	3.8	6.8	8.5	5.8	7.5
- property income	-11.5	0.8	-0.9	-13.5	20.2
- social benefits other than social transfers in kind	9.6	4.6	8.0	3.4	1.3
- other current transfers	13.7	-9.0	4.1	8.0	7.4
Current expenditure	7.2	6.6	8.4	7.0	8.3
of which:					
- property income	-5.7	1.7	15.1	2.0	48.3
- current taxes on income. wealth. etc.	7.1	5.9	8.2	9.4	12.6
- social contributions	8.2	6.8	8.9	6.5	7.6
- other current transfers	6.9	8.5	4.7	7.2	-1.9
Gross disposable income	4.1	5.3	5.6	3.1	4.7
Change in net equity of households in pension funds reserves	24.6	23.9	22.6	16.1	-8.9
Individual consumption expenditure	6.0	6.4	3.5	4.2	5.2
Gross saving	-11.7	-4.7	31.8	-6.3	-3.0
Gross savings rate	8.77	7.93	9.90	9.00	7.42
(gross saving/gross disposable income - ratio in per cent)					

B. AVERAGE WAGES

annual percentage changes

	2000	2001	2002	2003	2004
	Q1 - 4	Q1 - 4	Q1 - 4	Q1 - 4	Q1
Whole-economy nominal wage	5.9	8.1	7.0	6.4	8.0
Business sector	6.9	7.7	6.3	5.5	7.6
Non-business sector	2.6	9.6	9.8	9.8	9.7
Whole-economy real wage	1.9	3.2	5.1	6.3	5.6
Business sector	2.9	2.9	4.4	5.4	5.2
Non-business sector	-1.3	4.7	7.9	9.7	7.2

Note: including data for the Ministry of Defence and the Ministry of the Interior and an estimate for intelligence services not included in the survey.

C. UNEMPLOYMENT

end of period

	2000	2001	2002	2003	2004
	12	12	12	12	6
Registered job applicants (thousands)	457.4	461.9	514.4	542.4	517.5
Unemployment rate (percentages)	8.8	8.9	9.8	10.3	9.9

Source: CZSO

PRODUCER PRICES

percentage changes

	2000	2001	2002	2003	2004
					6
INDUSTRIAL PRODUCER PRICES					
a) previous month = 100	0.4	0.1	-0.1	0.1	1.1
b) same period of last year = 100	4.9	2.9	-0.5	-0.3	6.2
c) average for 2000 = 100	0.0	2.8	2.3	1.9	7.6
d) December 1999 = 100	3.4	6.3	5.8	5.4	11.3
CONSTRUCTION WORK PRICES					
a) previous month = 100	0.4	0.3	0.2	0.2	1.0
b) same period of last year = 100	4.0	4.1	2.7	2.2	3.5
c) average for 2000 = 100	0.0	4.1	6.9	9.2	12.9
d) December 1999 = 100	2.3	6.5	9.3	11.7	15.5
AGRICULTURAL PRODUCER PRICES					
b) same period of last year = 100	9.2	8.4	-9.5	-2.9	10.6
of which:					
crop products					
b) same period of last year = 100	12.6	9.3	-4.6	-1.0	17.0
livestock products					
b) same period of last year = 100	8.0	8.0	-12.1	-4.0	6.6
MARKET SERVICES PRICES (excluding interest rates)					
a) previous month = 100	0.4	0.1	0.3	0.0	-0.5
b) same period of last year = 100	3.4	3.9	3.2	1.6	2.6
c) average for 2000 = 100	0.0	4.0	7.3	9.0	11.8
d) December 1999 = 100	0.6	4.6	8.0	9.7	12.5

Source: CZSO

Table 22

RATIOS OF KEY INDICATORS TO GDP

percentage ratios

	2000	2001	2002	2003
State budget balance	-2.1	-2.9	-1.9	-4.3
Public budgets balance	-2.9	-2.3	-0.5	-5.3
Public debt	16.4	22.3	23.4	27.3
Debt in convertible currencies	37.6	35.0	33.7	35.3
Trade balance 1)	-5.6	-5.0	-3.0	-2.7
Current account balance	-4.9	-5.4	-5.6	-6.2
M2	65.7	68.9	68.4	69.7

Note: ratio = indicator/GDP at current prices
1) Source: CZSO

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