CNB Forecast

(Monetary Policy Report Summer 2024 – update)

IMF/WB Annual Meetings

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Summer 2024 Forecast – Summary

- **Inflation** will be close to the CNB's 2% target over the entire outlook, including the monetary policy horizon.
- **Economic growth** is continuing to recover at a moderate pace. It will be driven mainly by accelerating **household consumption** this year. Next year, **investment** will also start to grow again amid recovering external demand and falling domestic and foreign rates.
- **Nominal wage growth** will remain elevated from the long-term perspective.
- **Real household income** started to grow again in year-on-year terms at the start of this year; its previous declines will be offset only partially.
- Consistent with the summer forecast is a modest decline in **market interest rates.**

	2024	2025	2026
Headline inflation (%)	**2.2**	**2.0**	**2.0**
	(-0.1)	(-0.0)	-
GDP (%)	**1.2**	**2.8**	**2.4**
	(-0.2)	(0.1)	-
Average nominal wage (%)	**7.4**	**6.4**	**5.2**
	(0.2)	(0.3)	-
3M PRIBOR (%)	**5.1**	**3.8**	**3.3**
	(0.1)	(0.3)	-
Exchange rate (CZK/EUR)	**25.1**	**25.0**	**24.7**
	(0.0)	(0.2)	-

Presentation Outline

1. **Structural Changes and New Equilibria**
2. Assumptions of the Forecast
3. The New Macroeconomic Forecast
4. Scoreboard Risks

Changes in the Czech Economy’s Equilibria

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- The summer forecast assumes a reduction **in potential GDP growth** and **a slower equilibrium pace of koruna appreciation**. These adjustments have been incorporated into the summer forecast through expert judgement. The autumn forecast will be prepared using a recalibrated model.
- The following shifts occur in the equilibrium year-on-year growth rates:

Variable	Former equilibrium	New equilibrium
GDP (inc. domestic components)	3%	2.5%
Productivity	3%	2.5%
Nominal wages	5%	4.5%
Koruna appreciation	1.5%	1%

- The shift in medium-term equilibria does not affect the growth of **exports** and **imports**. Their values were already reduced from 6.4% to 4.8% in the spring 2024 forecast during the transition to the updated core prediction model (g3+). At that time, the link between foreign trade growth and economic growth in the effective euro area was weakened.
- The equilibrium growth of **foreign GDP** was reduced from 1.8% to 1.6% in 2019.

Structural Changes in the Czech Economy

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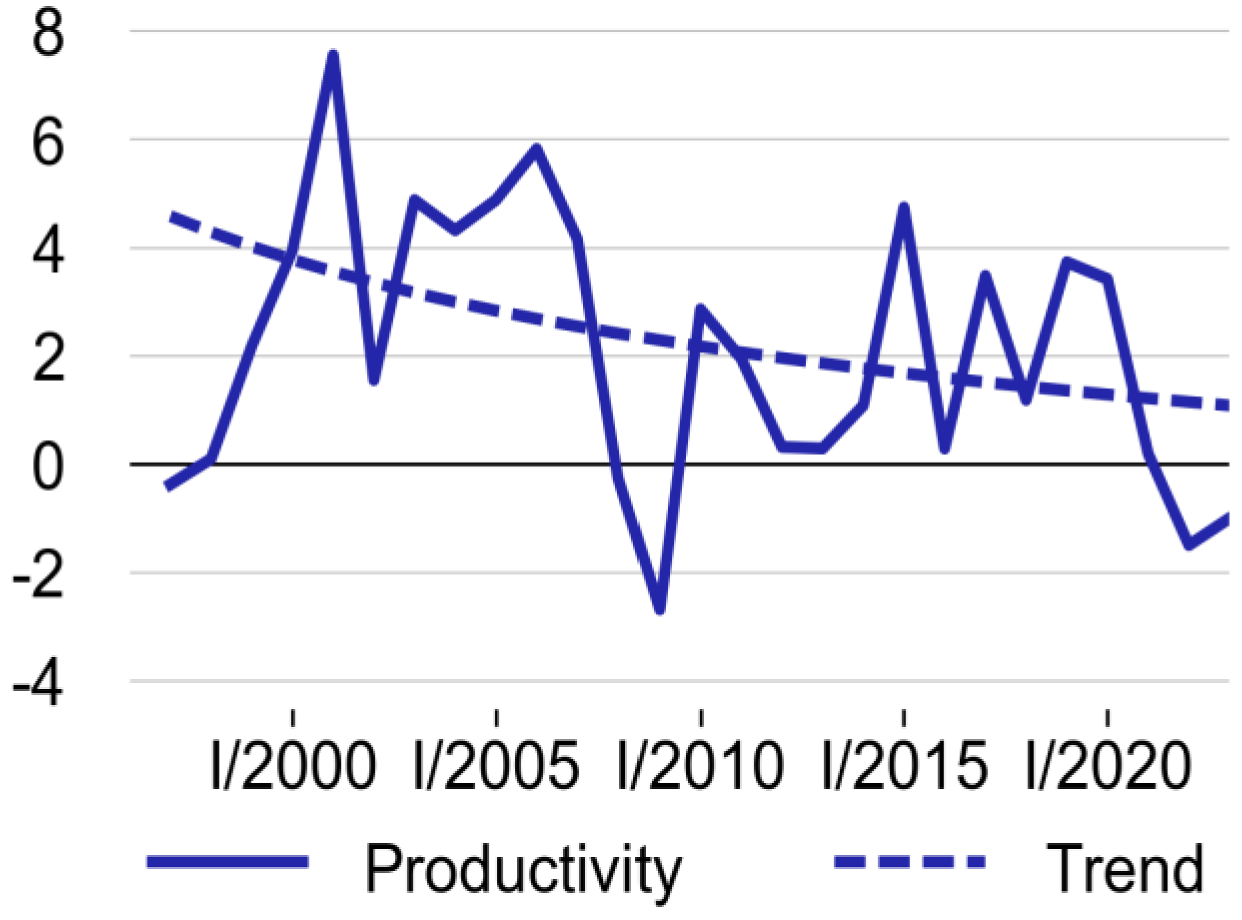
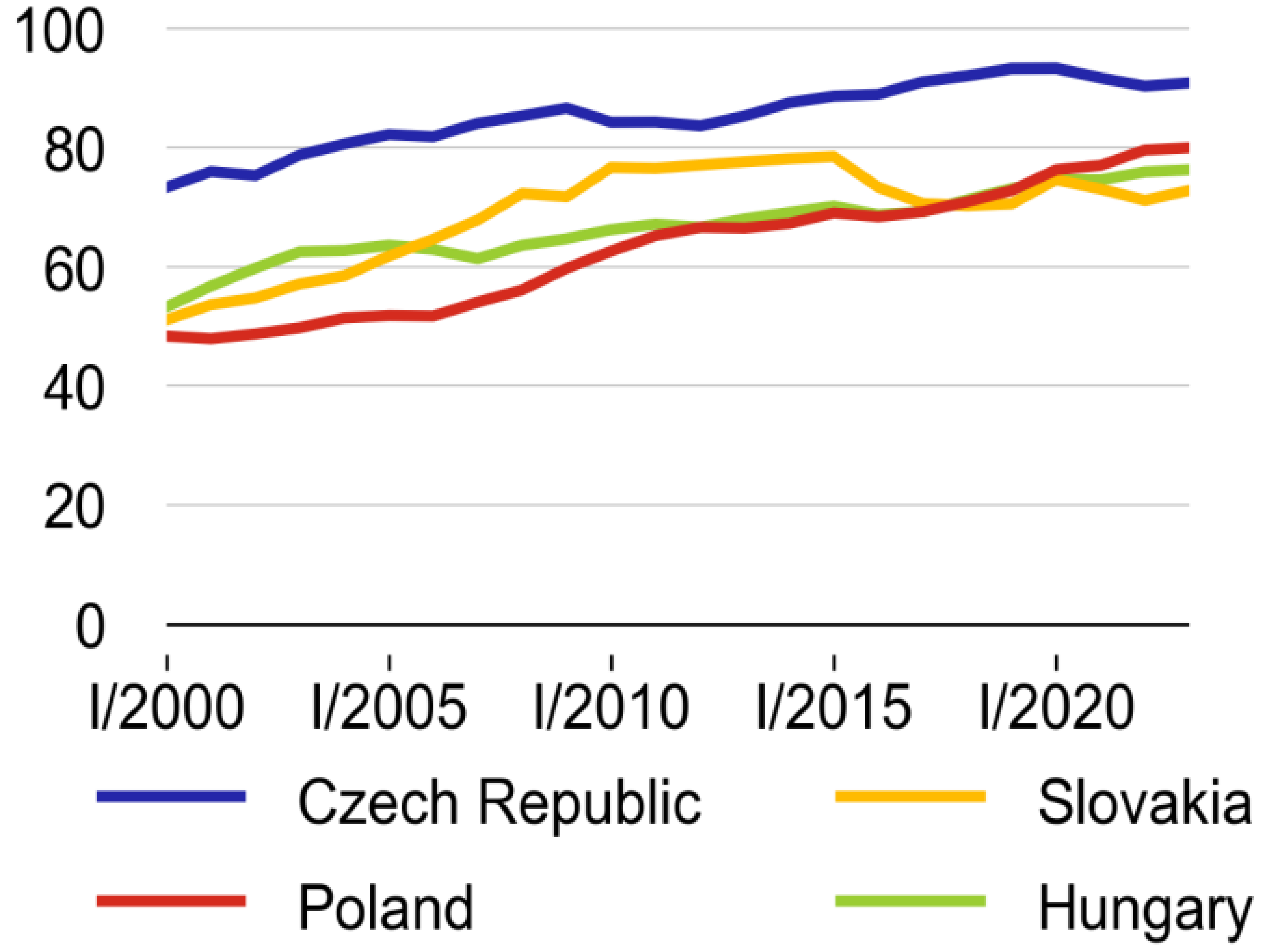
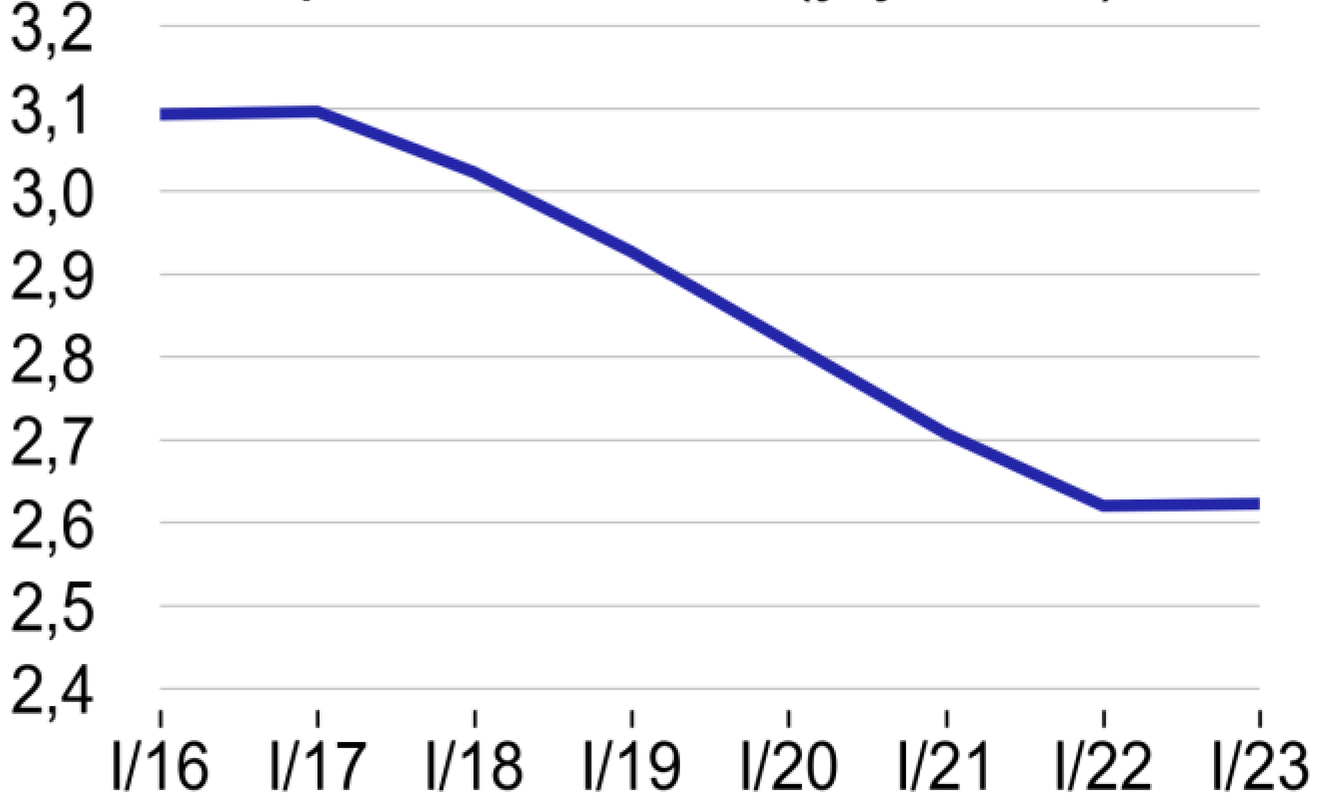
Productivity (y/y, in %)



Convergence to EU
(in % of EU real GDP per capita)



Solow-Swan model implied growth of potential GDP (y/y, in %)



CZK/EUR

- Based on a Chow test analysis of approximately 30 time series, we identified **structural changes in the Czech economy in 2016**.
- **Productivity growth** has long been slowing in the Czech economy.
- The **convergence** of the Czech economy to the EU average has slowed since 2016.
- The **growth of potential GDP** implied by the Solow-Swan model has decreased since 2016.
- The pace of **appreciation of the koruna** has slowed since the Global Financial and Economic Crisis.

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Foreign Environment Outlook

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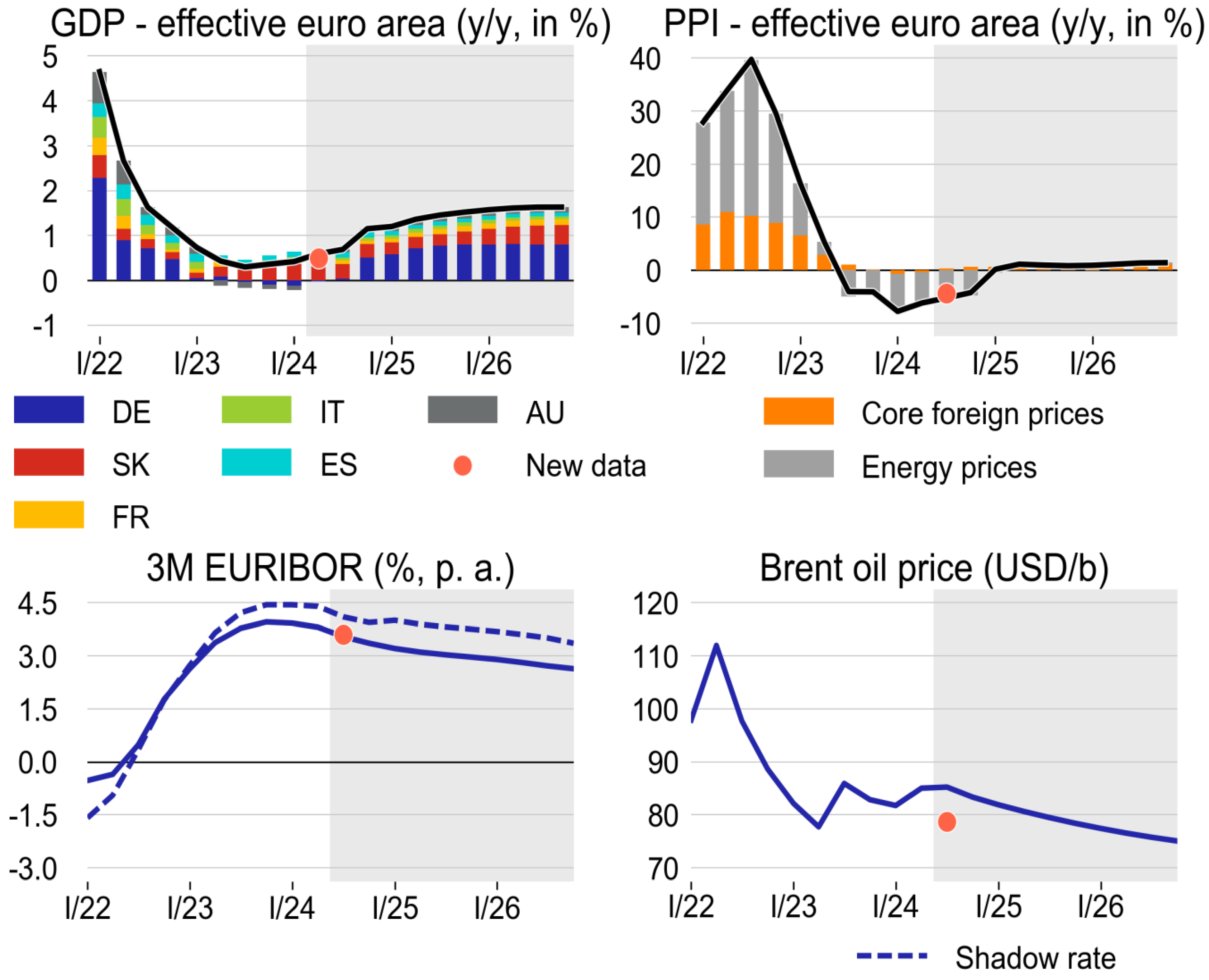
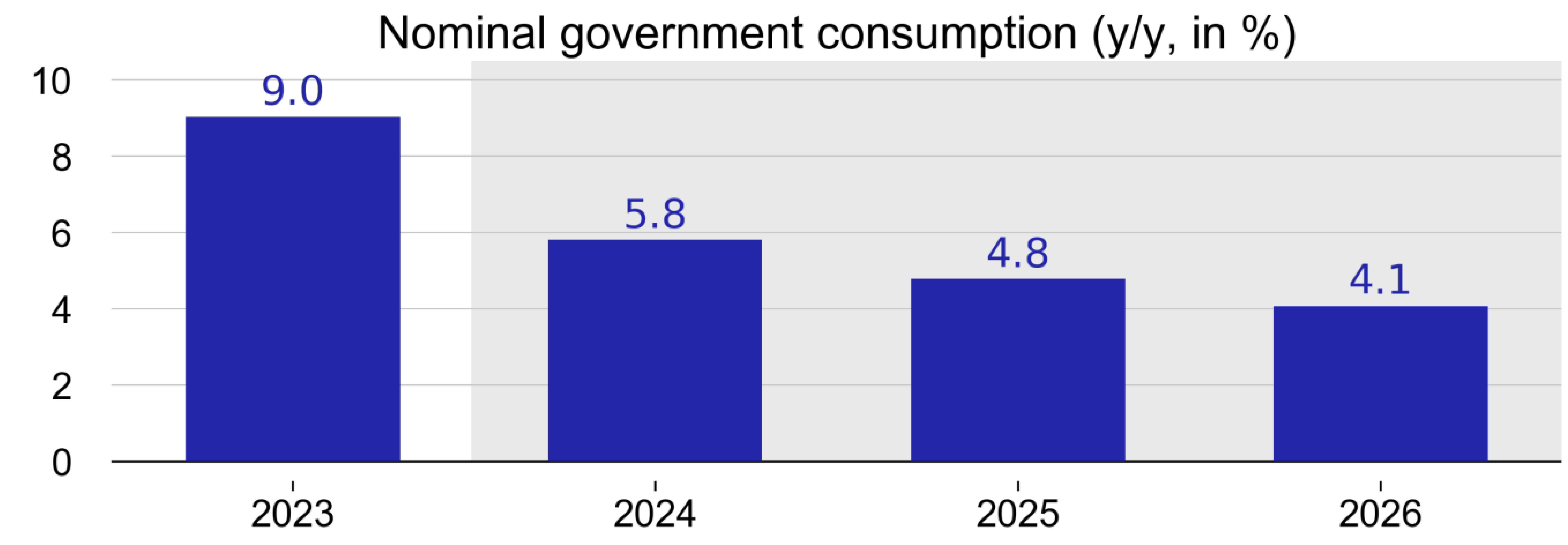
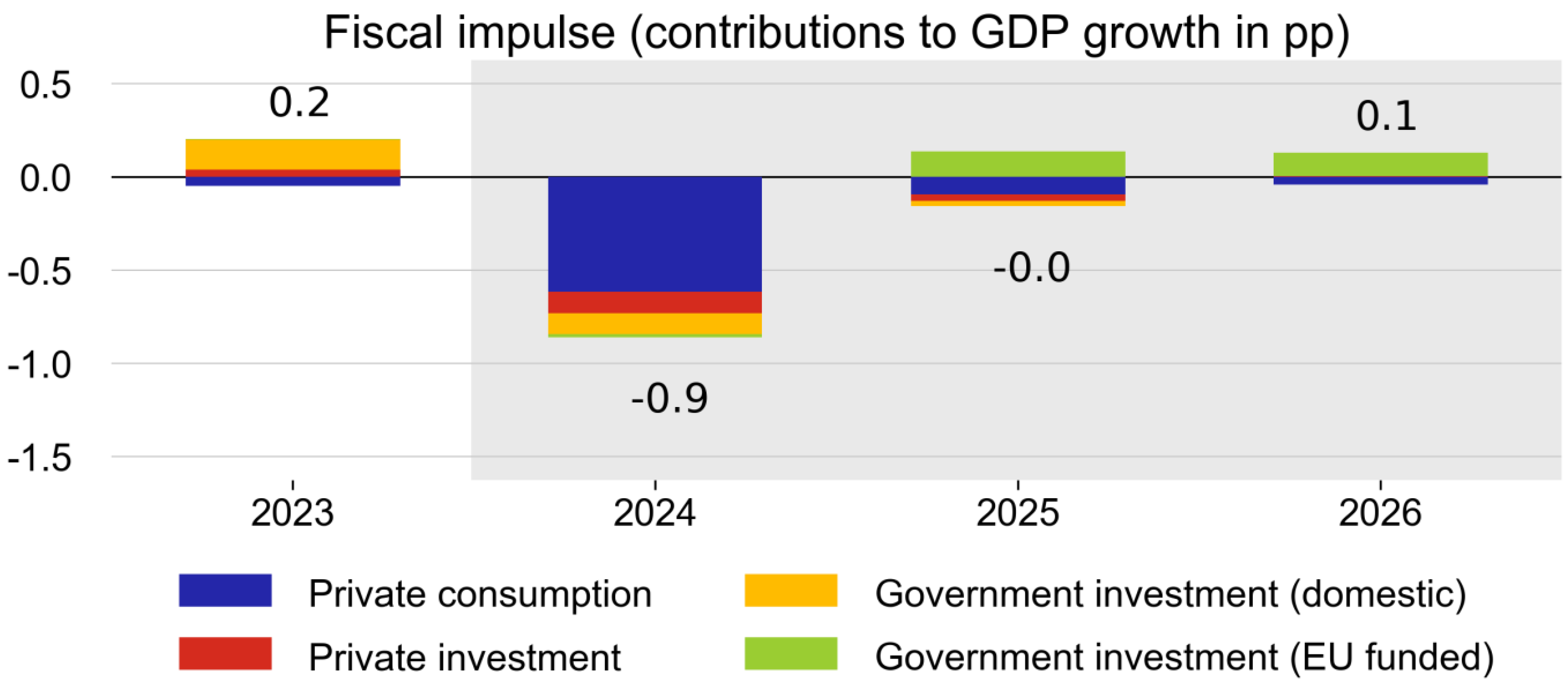


- **GDP growth in the effective euro area** will accelerate gradually, driven by the improving **performance of the German economy** as household consumption and global demand recover amid decreasing interest rates.
  - Czech exports to Germany are further analysed in the box *The position of Czech exporters on the German market by comparison with Poland.*
- **Industrial producer prices** will continue to fall this year, mainly because of their energy component, and will start to rise again in 2025.
- **Euro area interest rates** will go down further this year; the decline in the shadow rate will be dampened by an expected decrease in the rate of reinvestment by the ECB.
- The **Brent crude oil price** has risen since the start of this year, but its outlook remains falling.

Fiscal Policy





- Growth in **nominal general government consumption** will slow despite expected renewed brisk growth in public sector pay this year and the next.
  - Reduction in operating expenditure under the consolidation package;
  - Partial fade-out of last year’s effect of increased expenditure linked to the arrival of Ukrainian war refugees.
- **Fiscal policy** is significantly dampening GDP growth this year (due mainly to the consolidation package) and will have a neutral effect next year.

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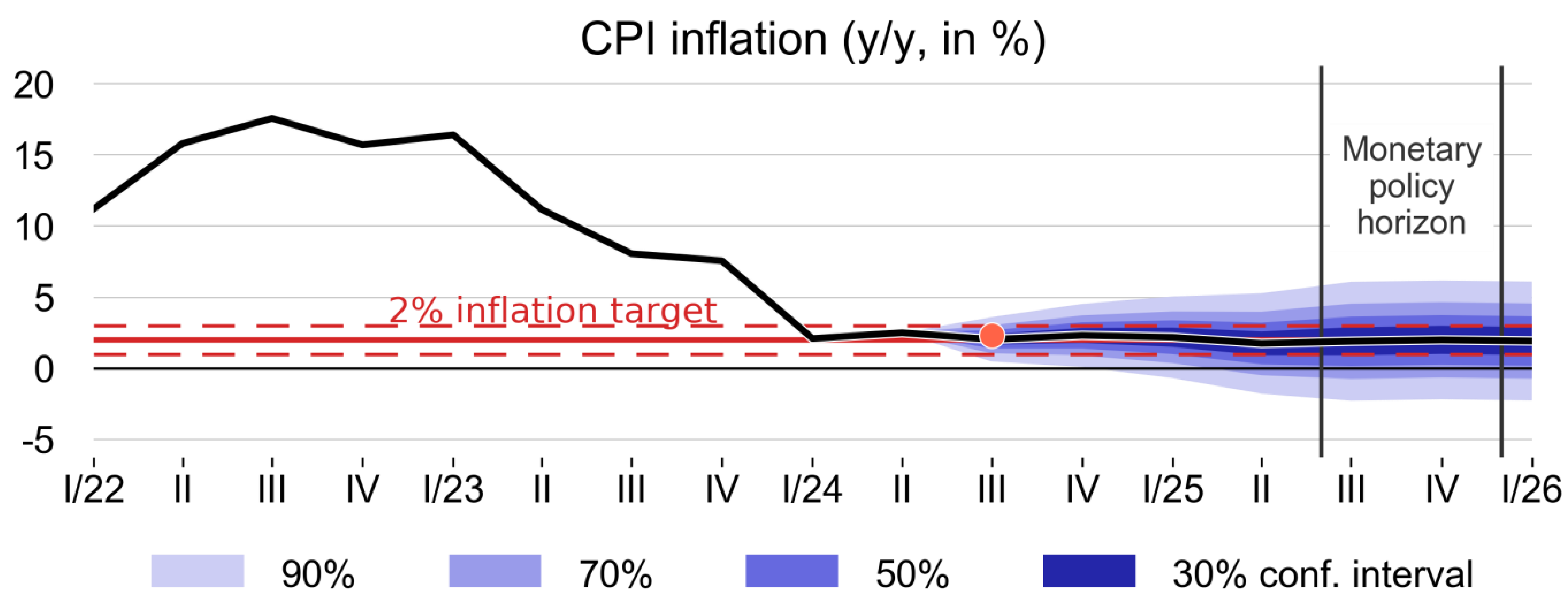
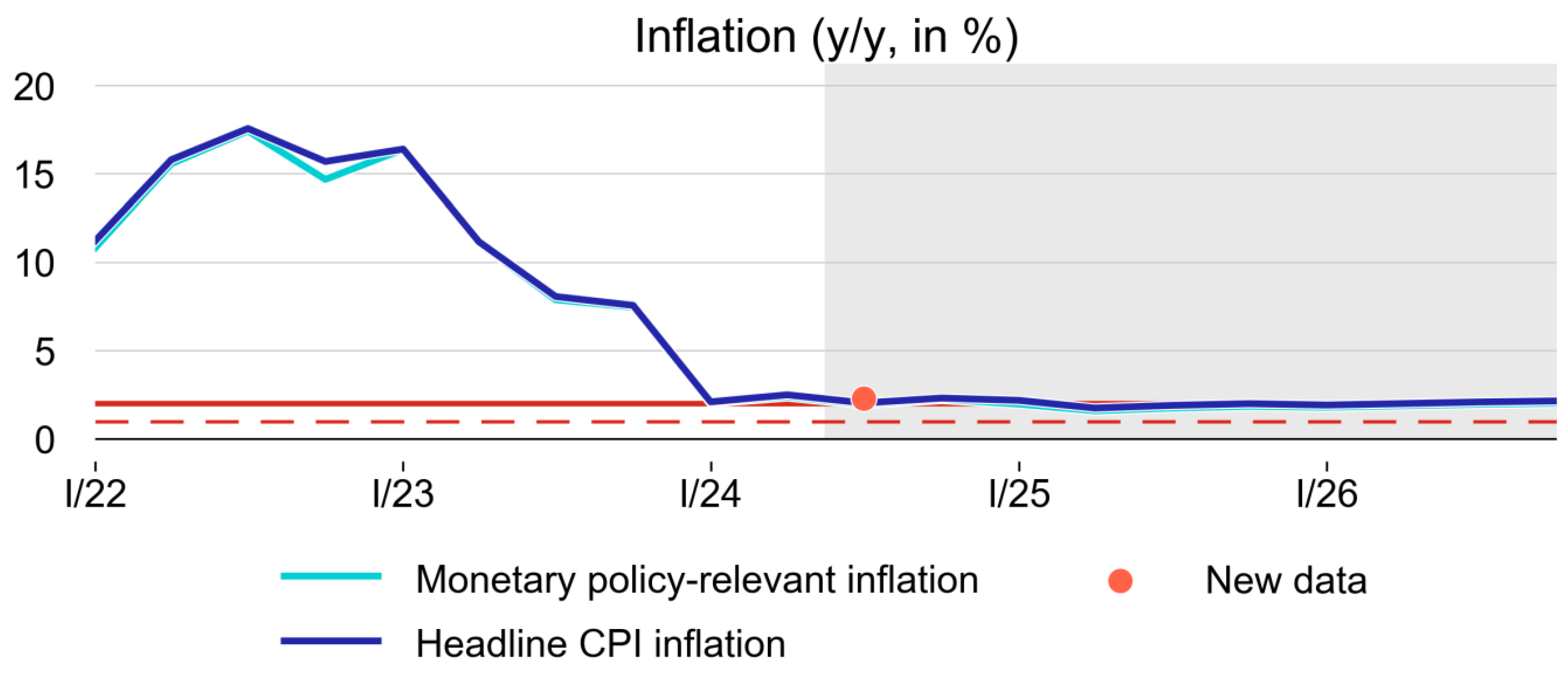
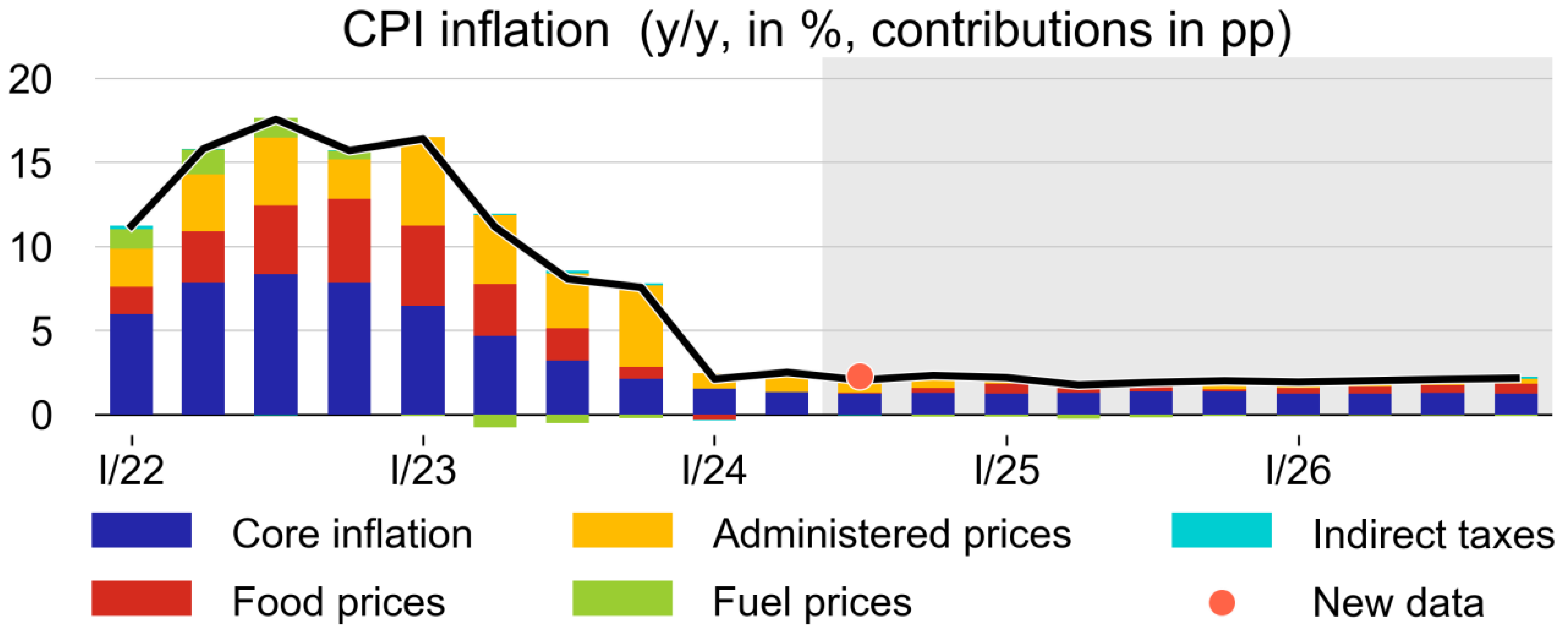
Headline and Monetary Policy-Relevant Inflation

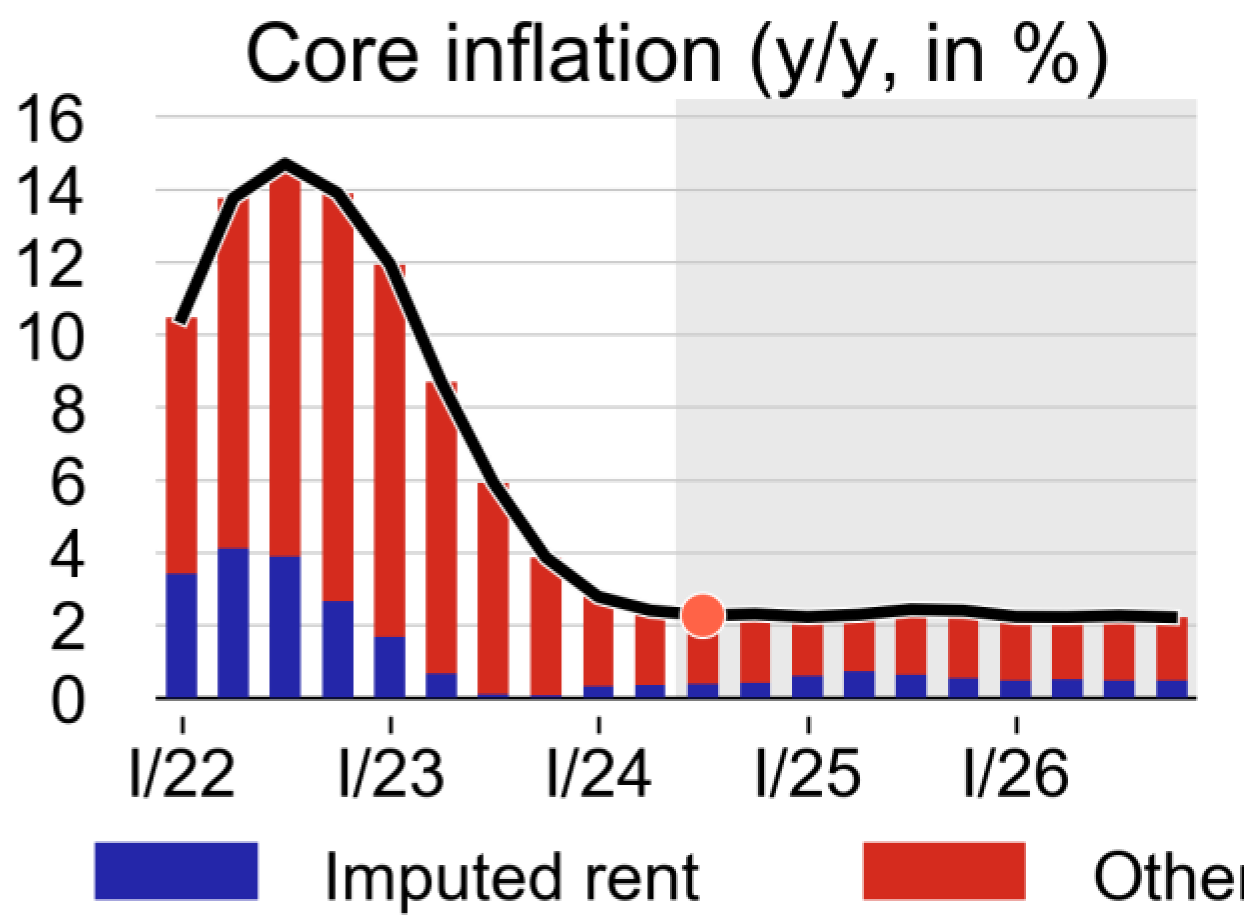


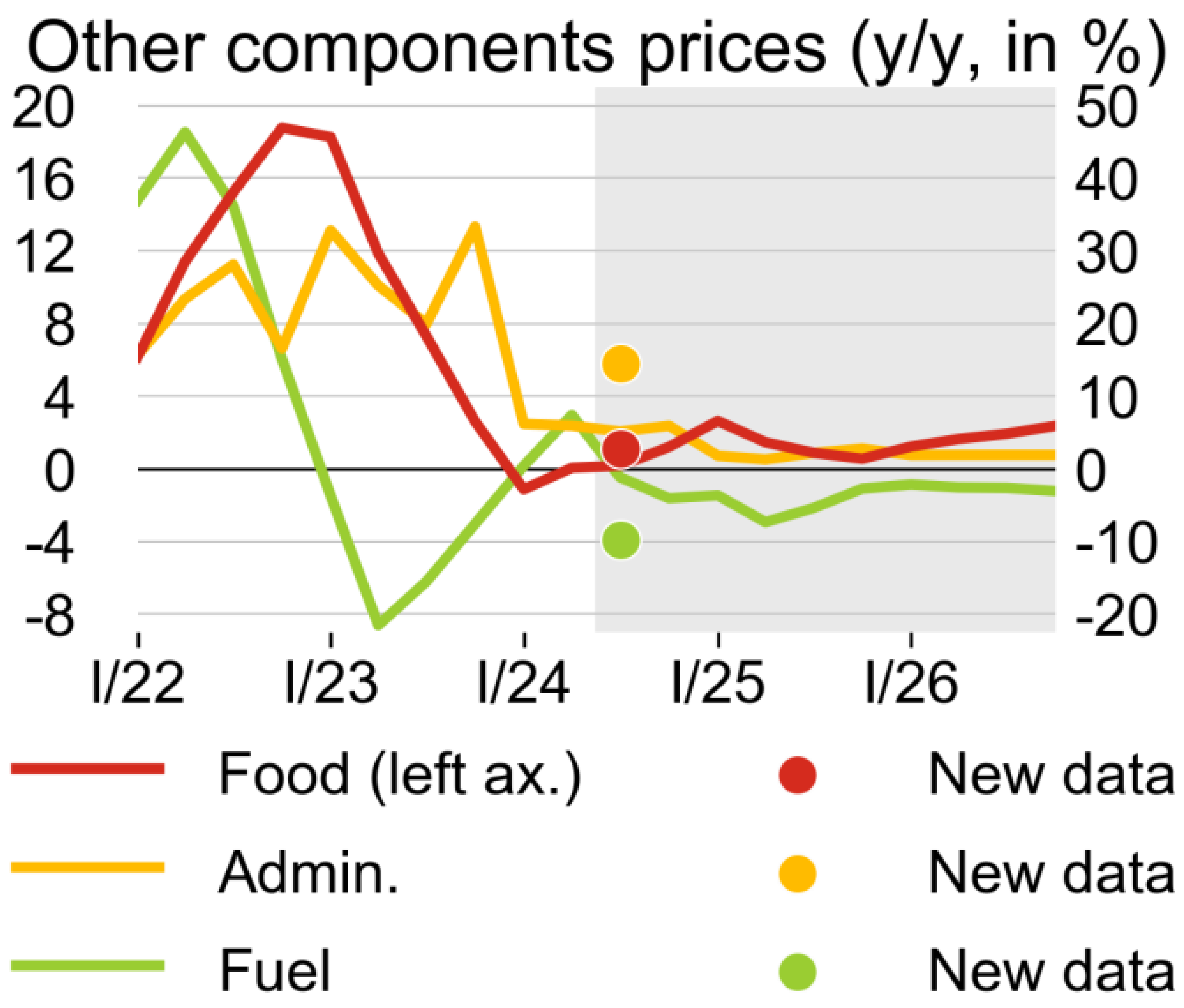


- **Inflation** will be close to the **2% target** for the rest of this year and stay there over the monetary policy horizon.
- Headline inflation will be slightly above **monetary policy-relevant inflation** due mainly to the slightly inflationary effect of the increase in excise duties on tobacco and alcohol.

CPI Inflation, Core Inflation and Administered Prices







- **Consumer price inflation** slowed sharply at the start of this year and was exactly at the CNB's 2% target in June. Inflation will fall slightly in Q3 due mainly to a lower contribution of core inflation and will be at the CNB's 2% inflation target on average.
- **Core inflation** will remain close to 2% amid a gradually increasing contribution of imputed rent.
- **Food price inflation** will accelerate at the end of Q3 and then also in Q4 due to base effects.
- **Administered price inflation** will decline to its long-term average in 2025.
- **Fuel price inflation** will be negative in the coming quarters, mainly because of a gradual correction of the currently somewhat elevated oil prices.

Cost Pressures and Profit Mark-ups

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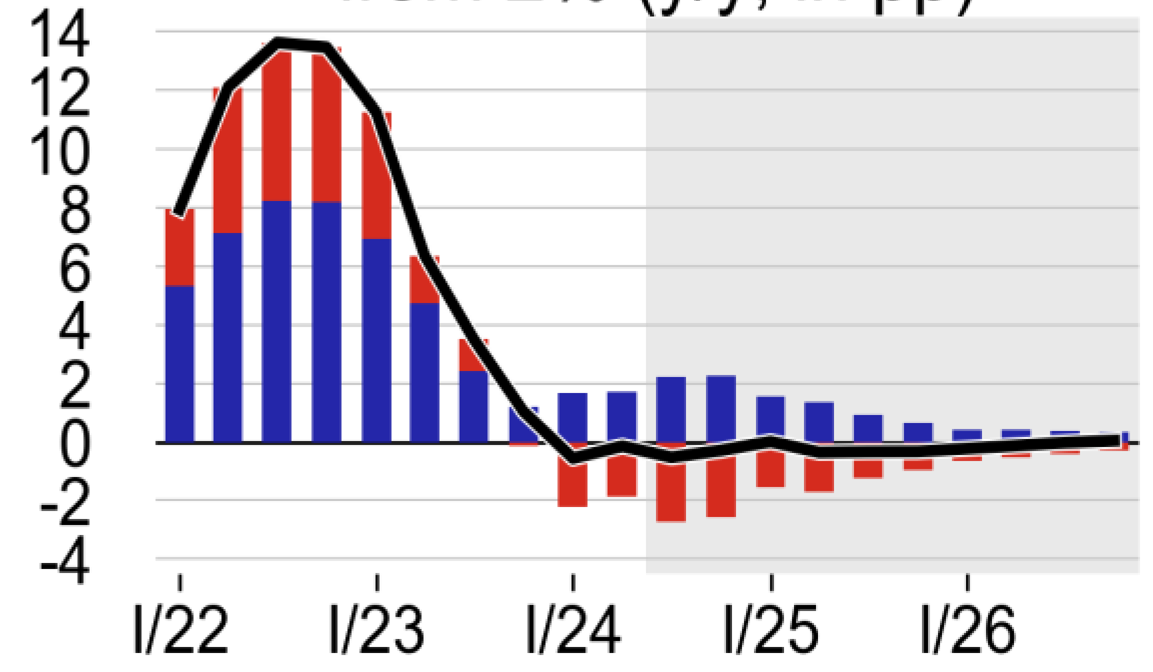
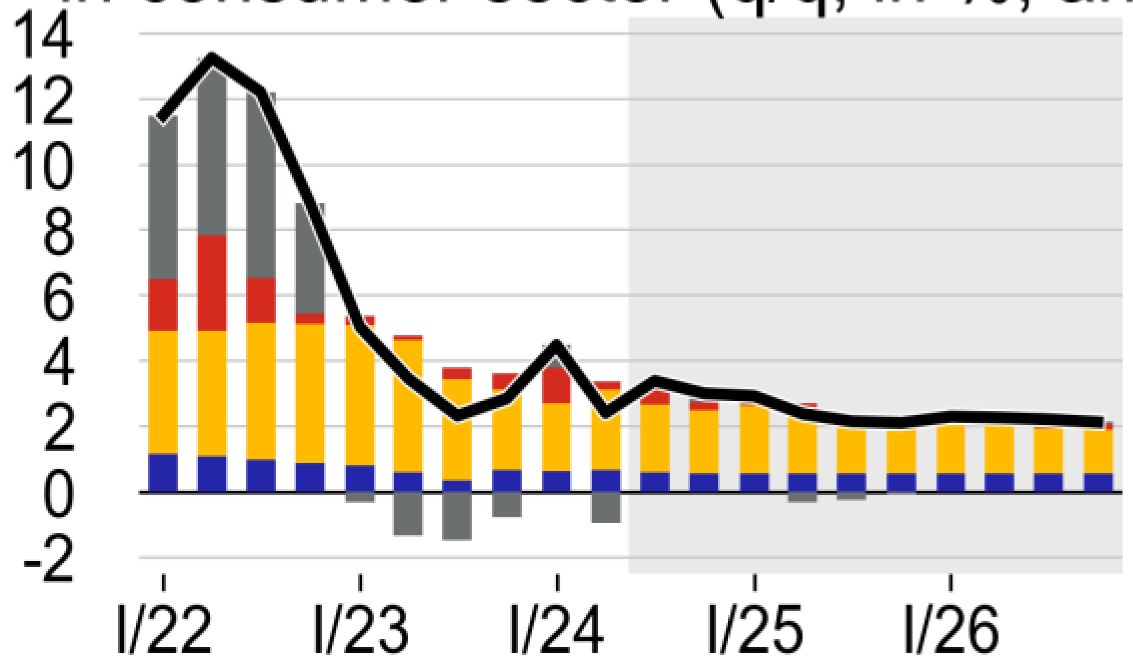
Deviation of market prices from 2% (y/y, in pp)



Costs

Surcharge to costs

Nominal marginal costs in consumer sector (q/q, in %, ann.)



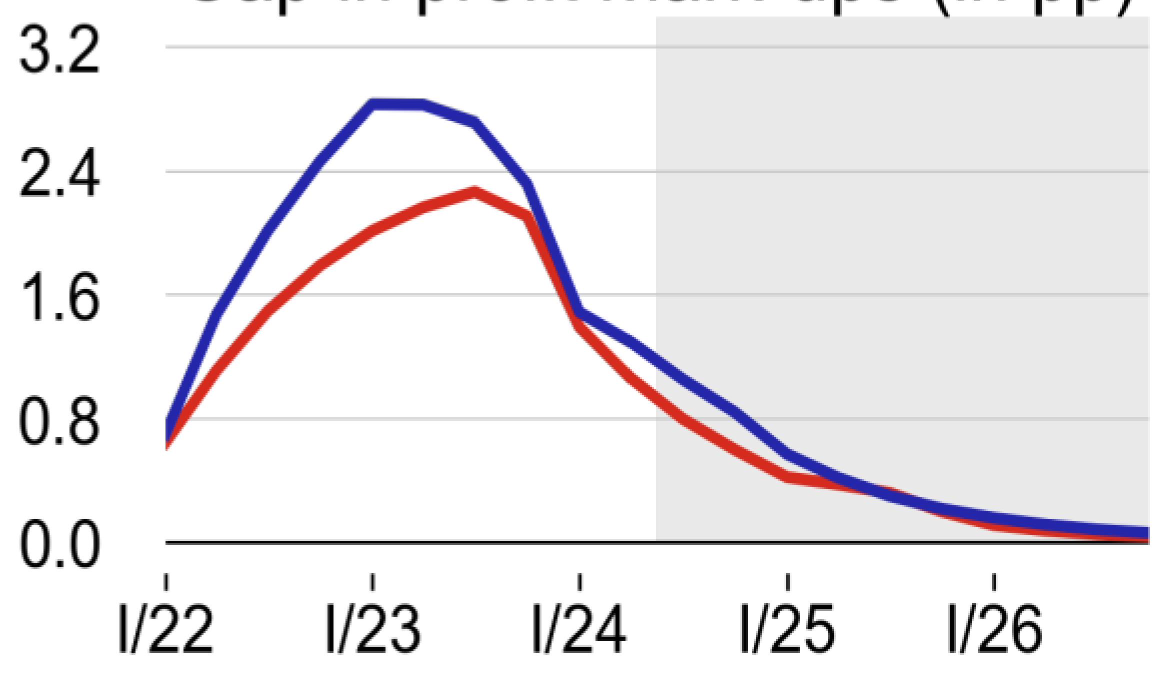
Price convergence

Interm. goods prices

Core imp. prices

Energy imp. prices

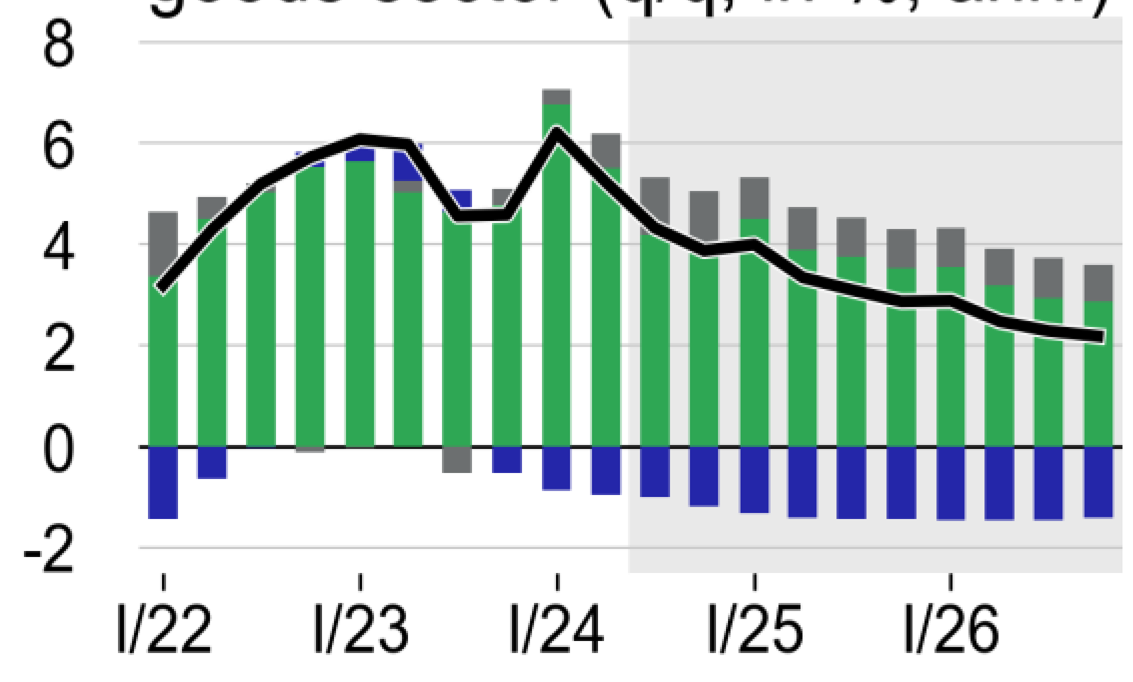
Gap in profit mark-ups (in pp)



Consumer Sector

Intermediate sector

Nominal marginal costs in intermediate goods sector (q/q, in %, ann.)



Wages in market sectors

Price of capital

Labor efficiency

- **Market price growth** over the past two years has been driven by rising costs and a price **surcharge**, which has gone well beyond the corresponding increase in **costs**.
  - This year, the contribution of the surcharge to costs turned negative. Despite continued elevated cost growth, retailers re-priced only to a limited extent due to the current tight monetary policy.
  - In the outlook, the surcharge to costs remains negative and costs will continue to contribute positively.
- The elevated **overall cost pressures** will decline next year amid a gradual reduction in the inflationary effect of the domestic economy and renewed gradual appreciation of the koruna.
- The **domestic cost pressures** will ease gradually over the outlook as quarter-on-quarter **growth in market wages** decreases.

Labour Market

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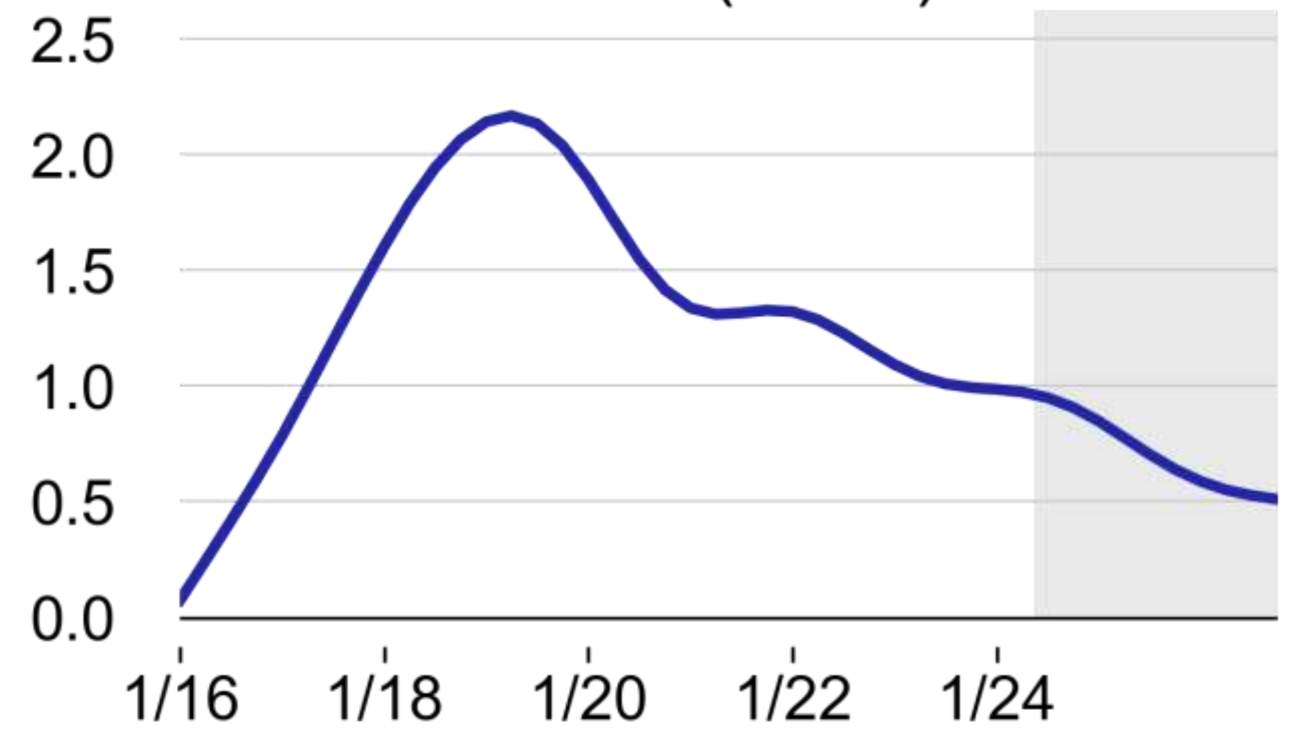
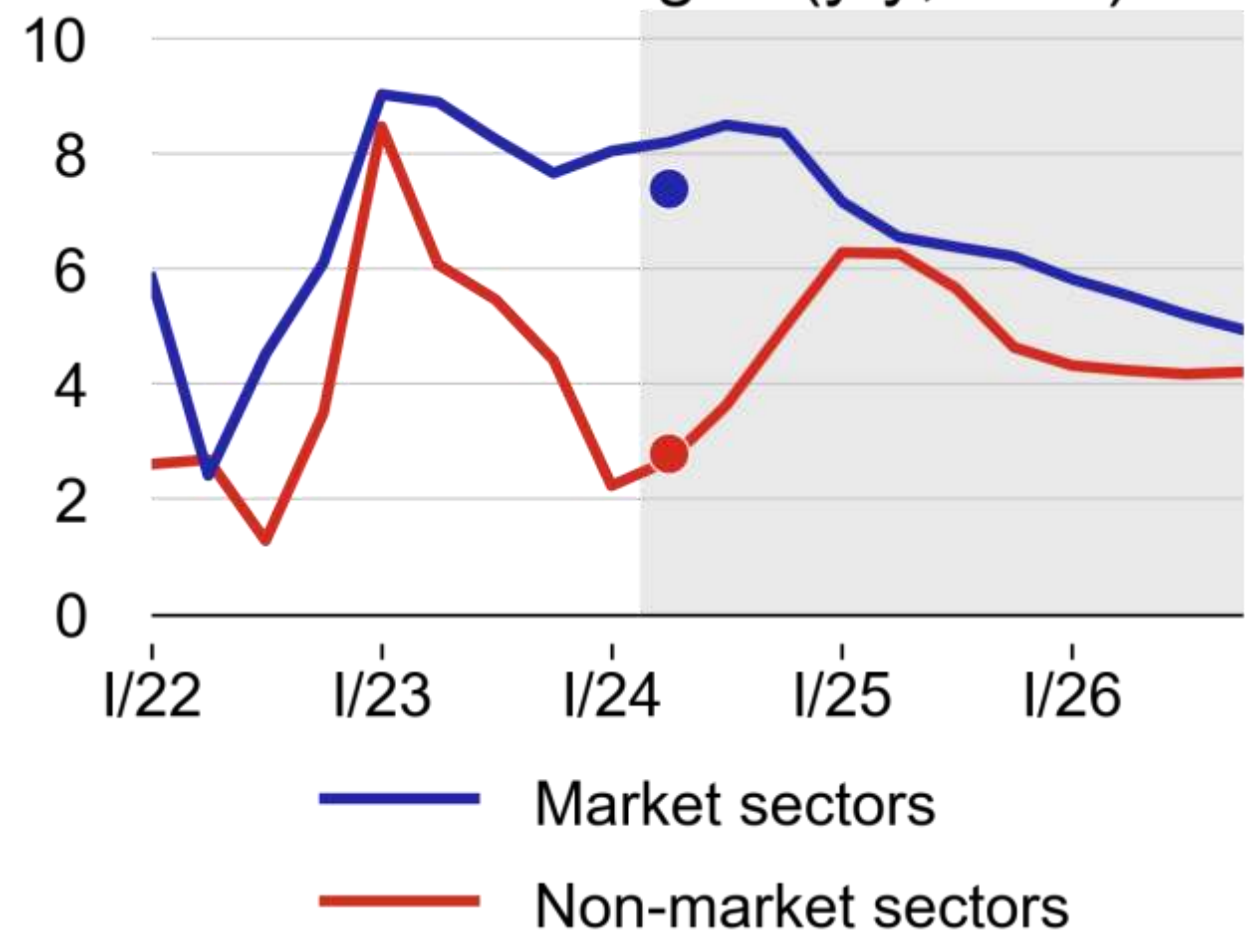
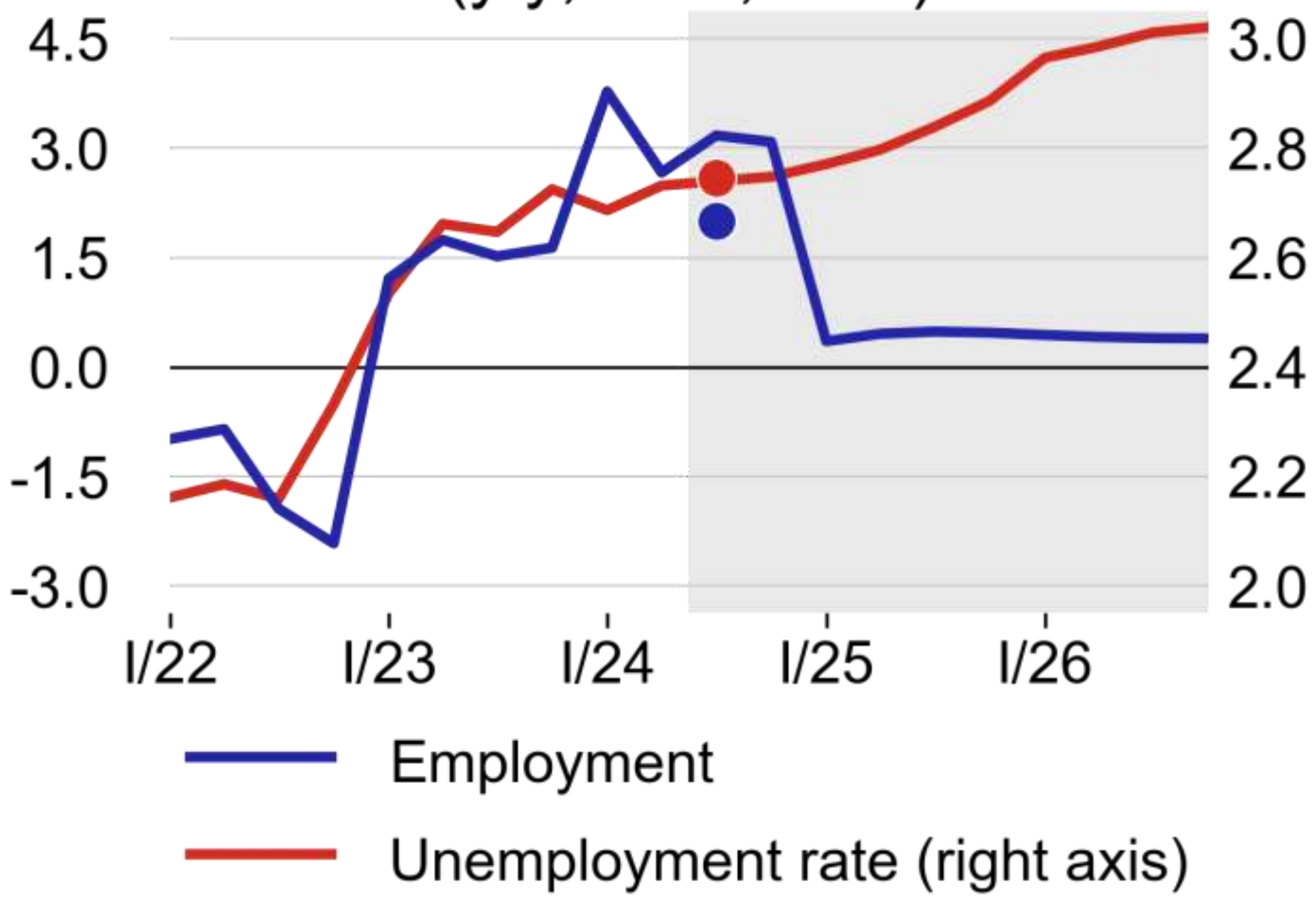
LUCI (index)



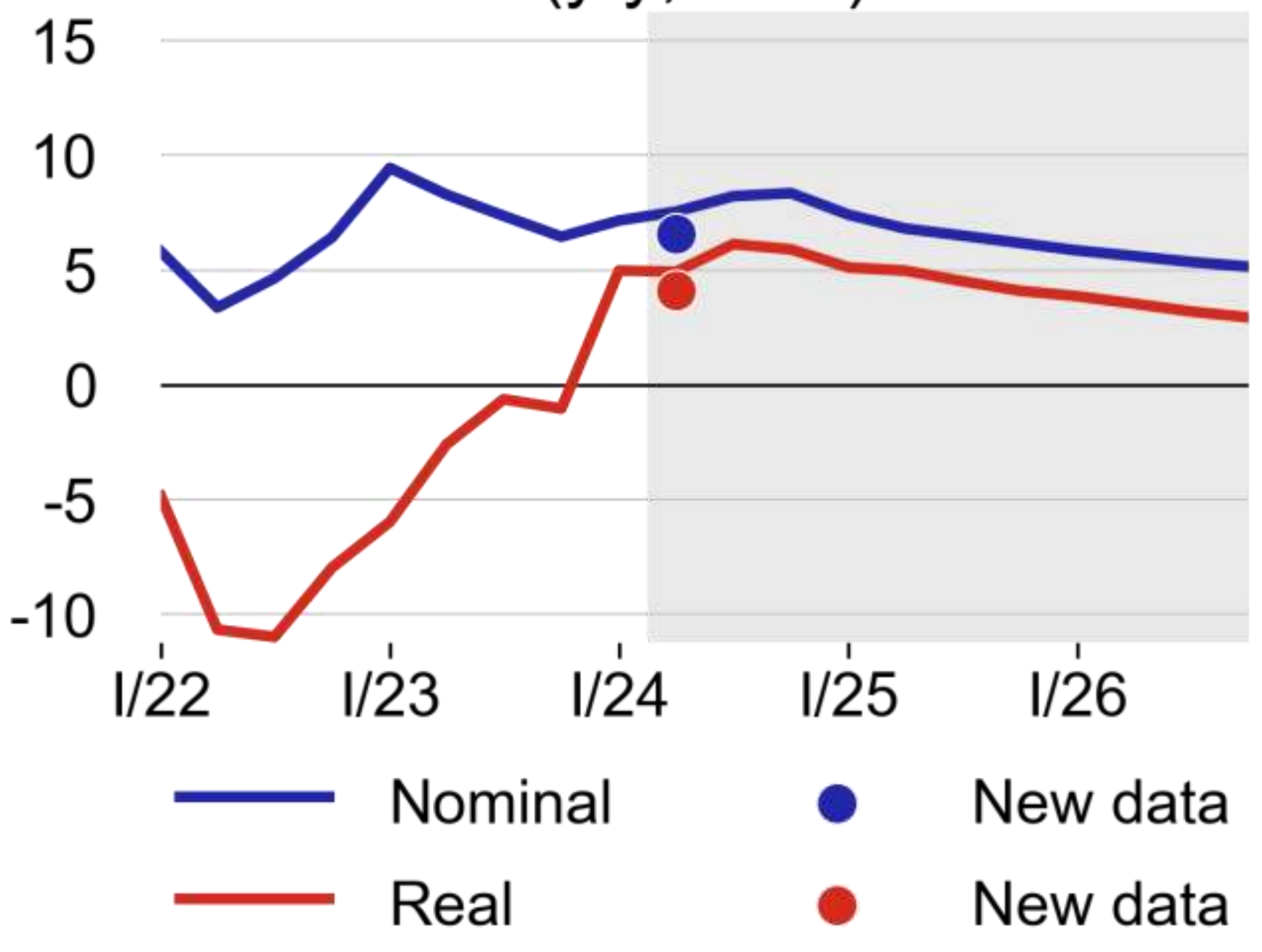
Nominal wages (y/y, in %)



Employment and unemployment rate (y/y, in %, s. a.)



Volume of wages and salaries (y/y, in %)



- From the perspective of the **LUCI**, the tightness in the labour market will gradually decrease further.
- **Nominal wage growth** will remain elevated from the long-term perspective and slow only gradually.
- **Employment** will surge this year due to a statistical effect at the start of the year; the **unemployment rate** will increase only slowly.
- The **real wage** has started to grow again and will continue to rise throughout the year, due mainly to a significant slowdown in inflation to close to the 2% target amid continued, solid nominal wage growth.
- Growth in the **real wage bill** will thus help household consumption to recover.

GDP Growth Forecast

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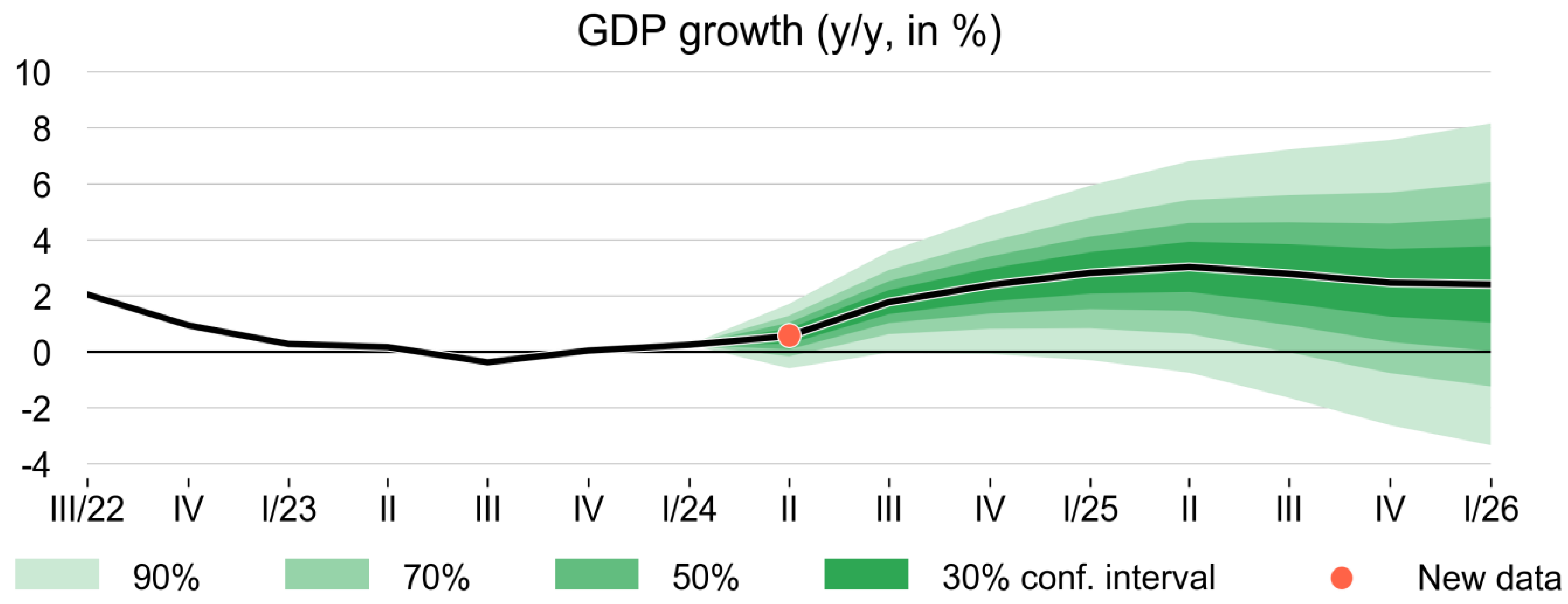
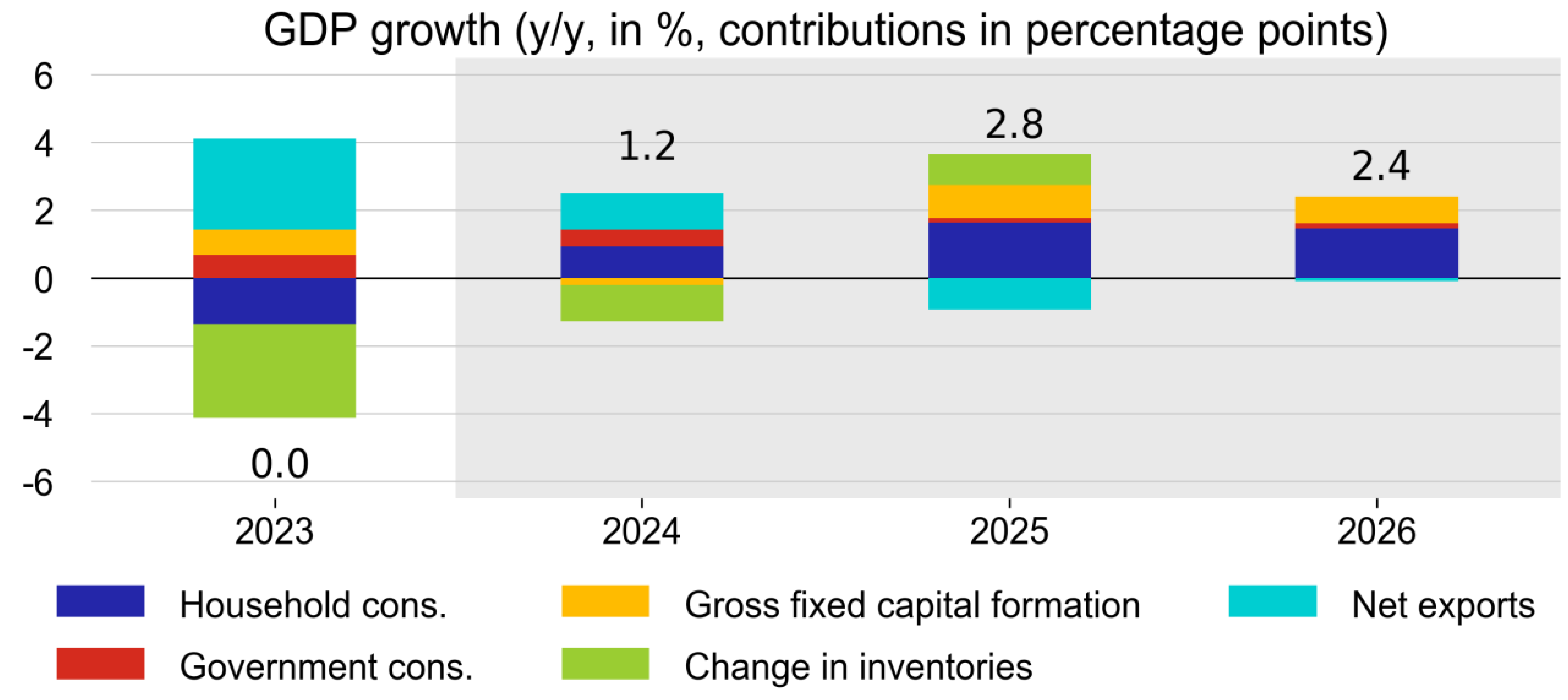
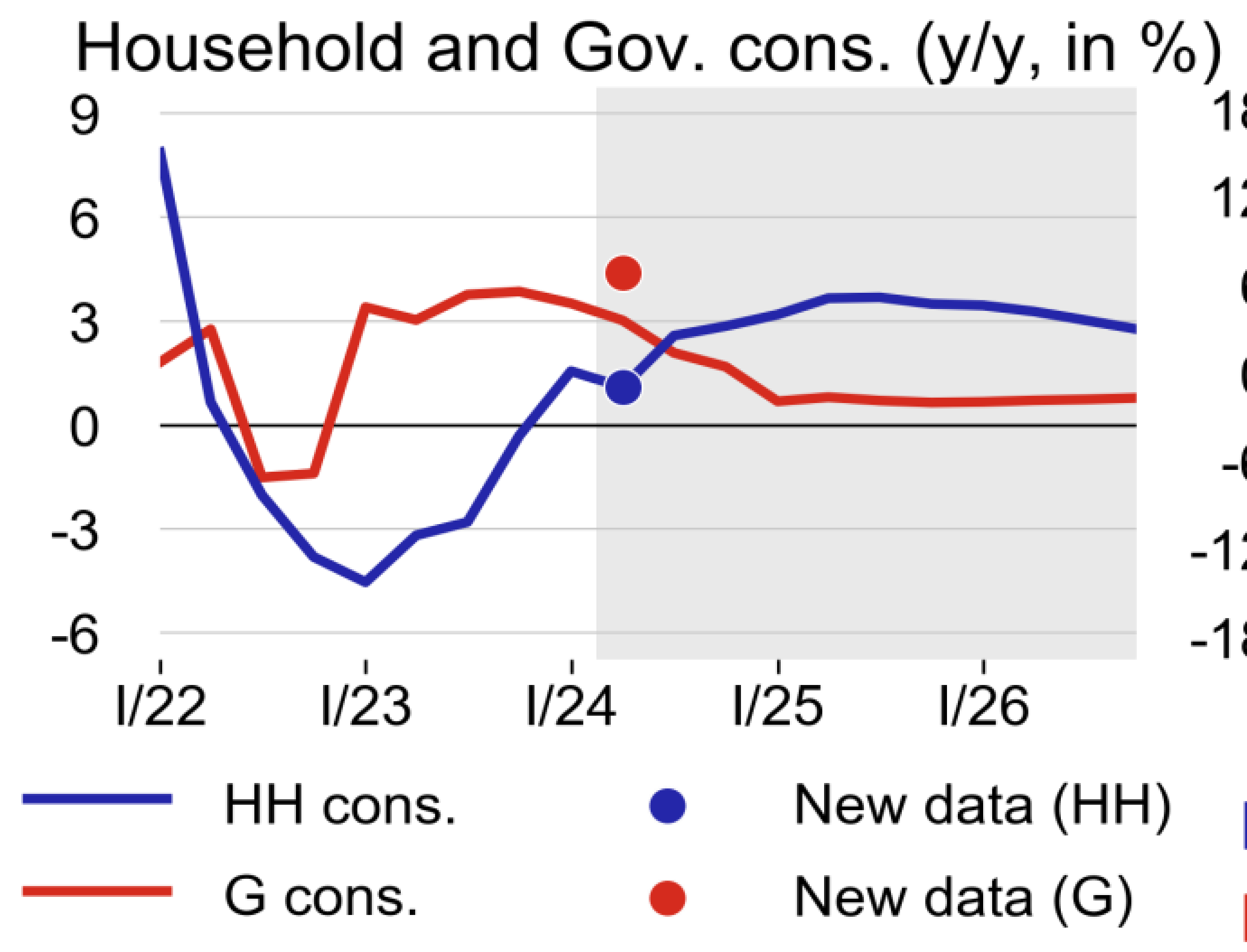
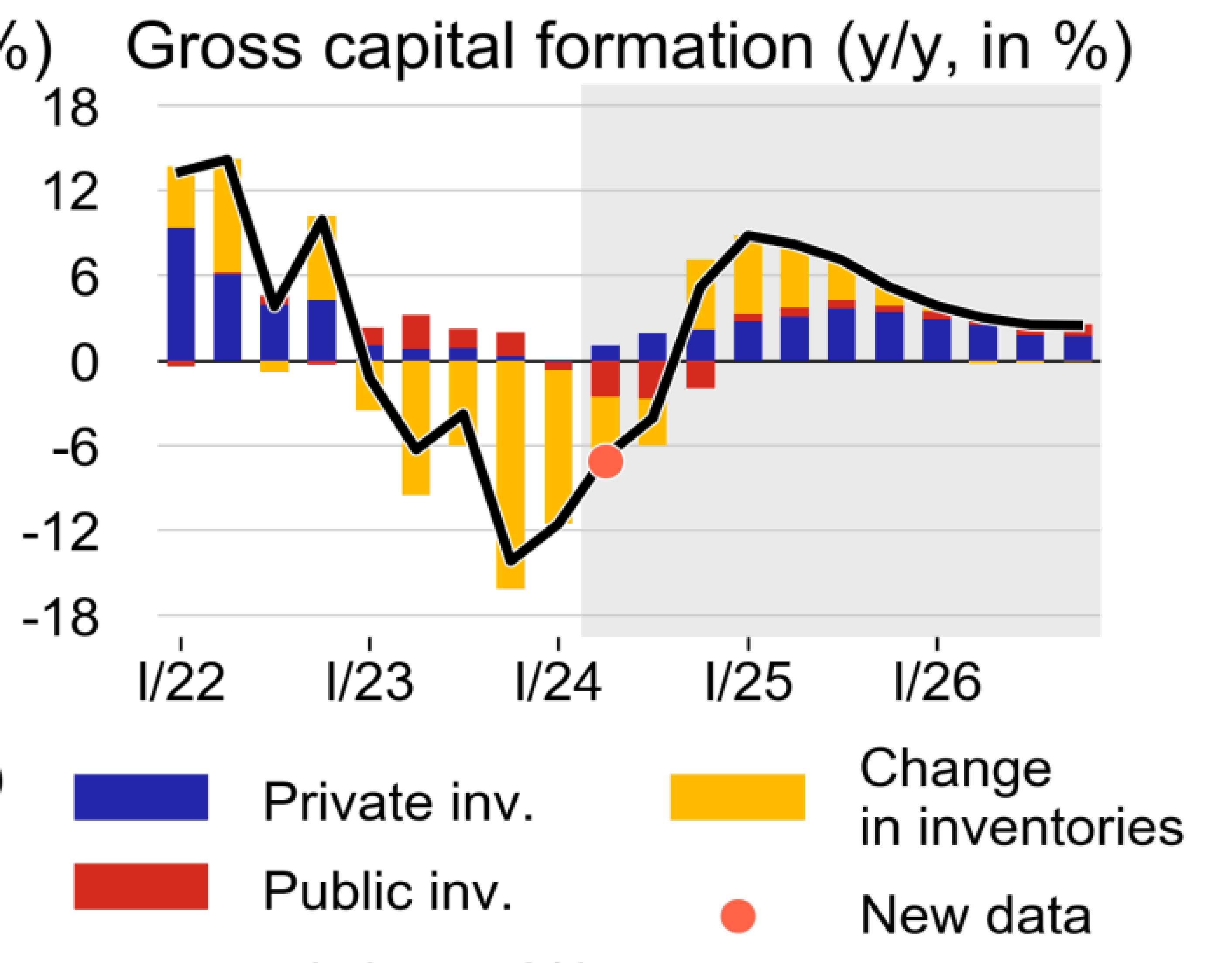


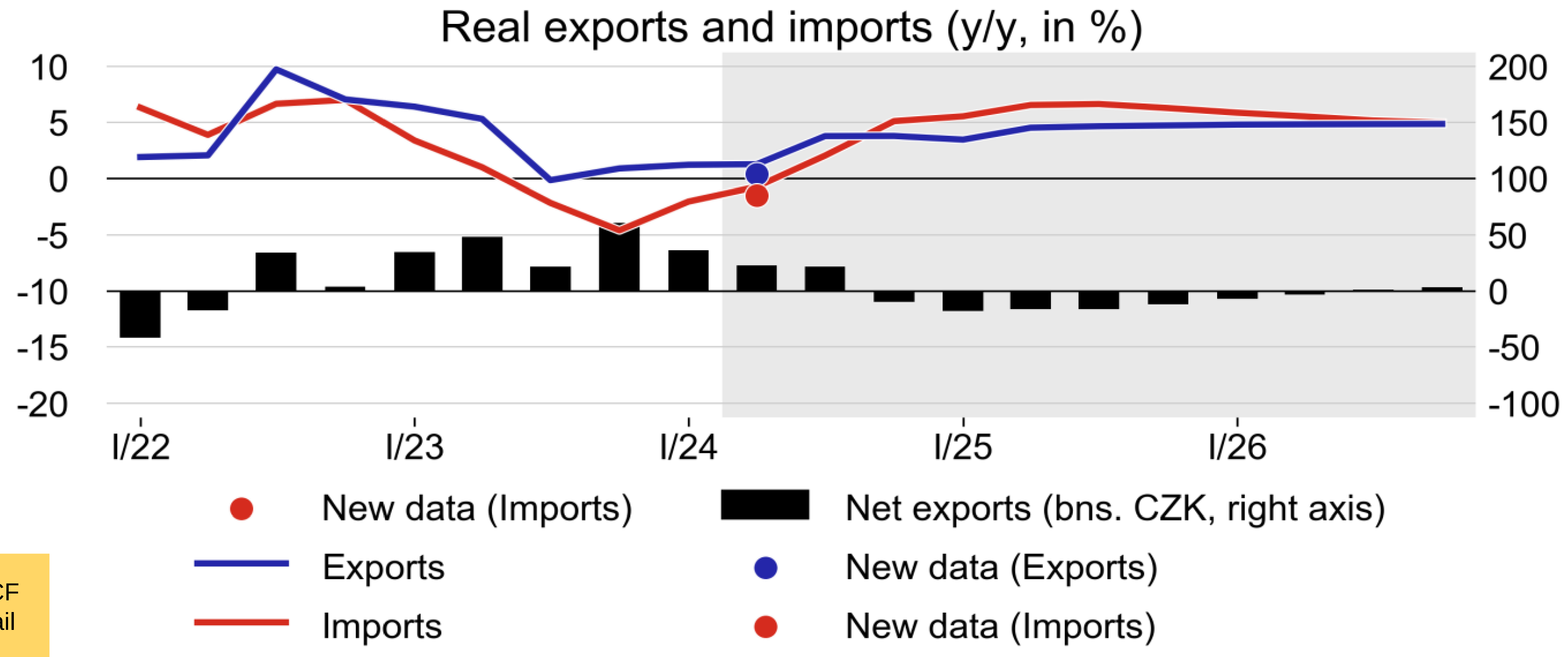


- The **economy** will expand this year and **GDP growth** will pick up further next year.
- In whole-year terms, **GDP** will grow by **1.2%**. In 2025, the growth will pick up to **2.8%**. It will slow to close to the new equilibrium of **2.5%** in 2026.
- According to a preliminary CZSO estimate, Czech GDP increased by **0.3%** quarter on quarter and by **0.4%** year on year in 2024 Q2. This is slightly lower than the CNB's forecast.

GDP Components



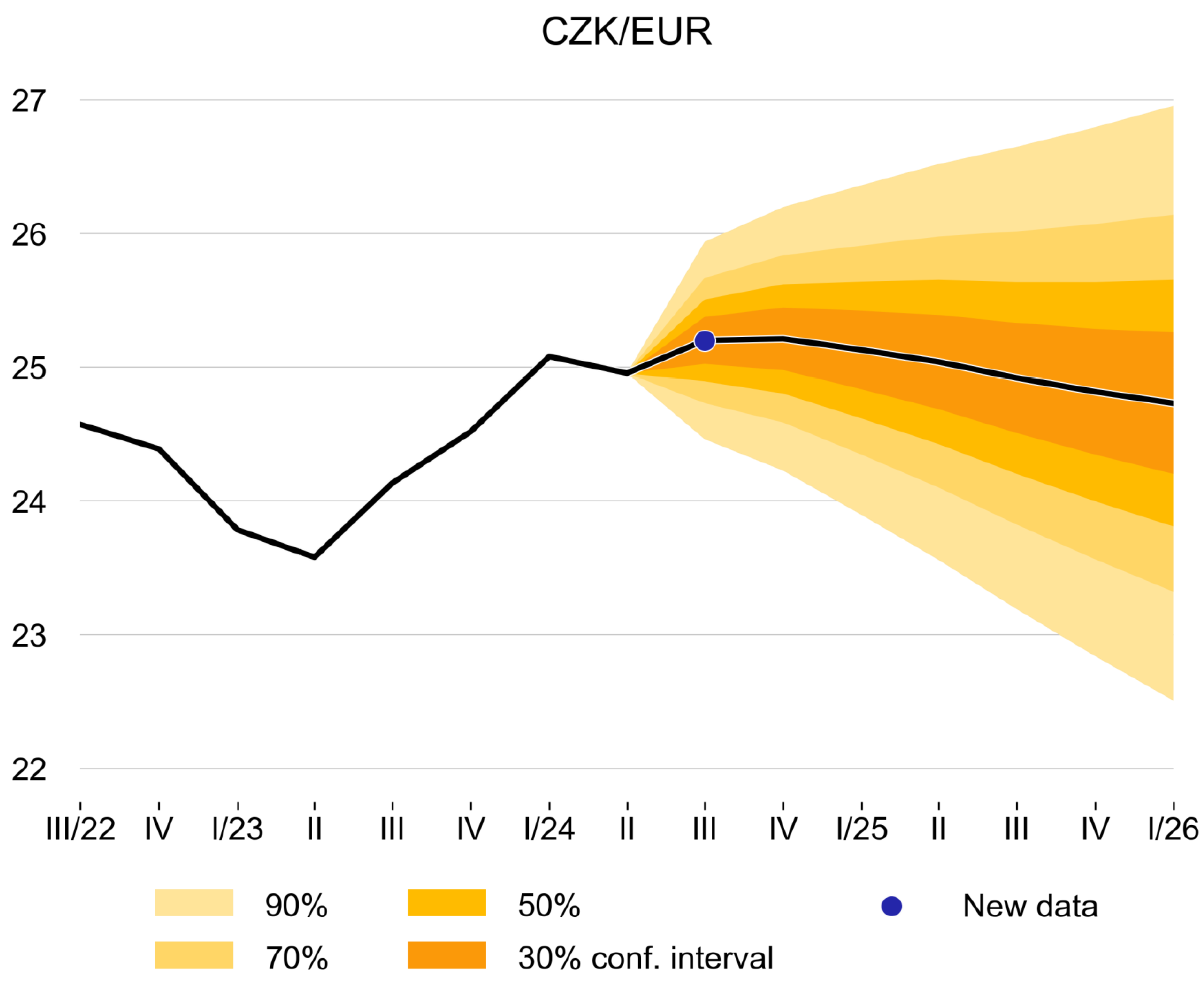




- Growth in **household consumption** will recover rapidly on the back of swiftly rising real wages.
- **Government consumption** will grow at a subdued pace.
- Growth in total **gross capital formation** will be volatile due to **inventories**, while growth in **private fixed investment** will accelerate gradually following an initial downturn.
- **General government investment** will decline this year due mainly to consolidation efforts.
- **Export** and **import** growth will gradually accelerate this year as external and domestic demand slowly recover.

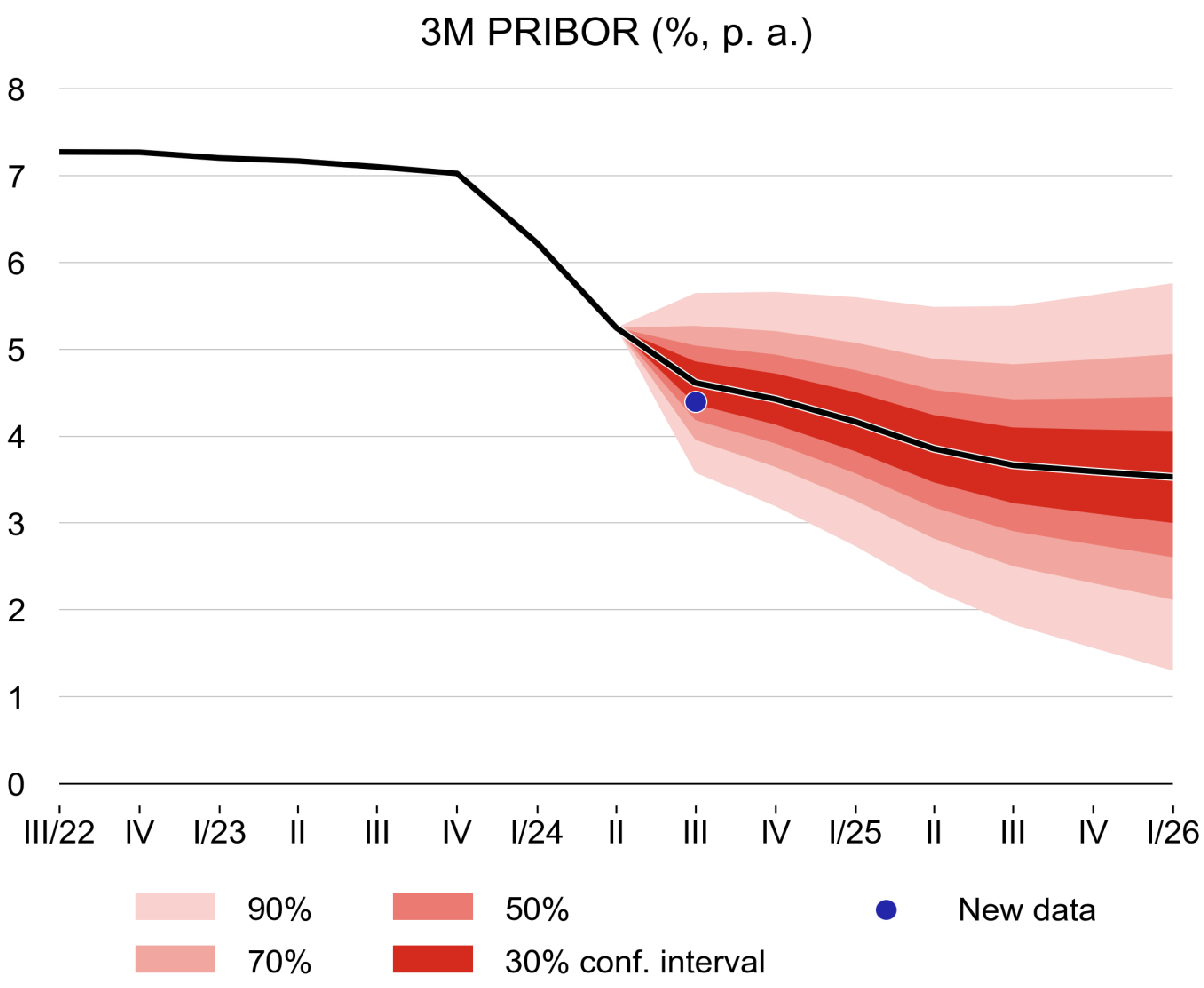
GFCF detail

Exchange Rate CZK/EUR



- The summer forecast expects the koruna to average **CZK 25.2** to the euro in 2024 Q3.
- After broadly stagnating at the end of this year, the koruna will start to appreciate slightly, due mainly to favourable **net exports** of goods and services and continued **growth in economic activity**.
- The appreciation of the koruna will be dampened by a gradually narrowing **interest rate differential** vis-à-vis the euro area.

Interest Rate Path (3M PRIBOR)



- Consistent with the baseline scenario is a modest decline in **market interest rates**.
- Although growth in costs will still be slightly elevated this year due to the repercussions of the previous extraordinary inflation pressures, this will not reverse the need to ease monetary policy further.
- The inflationary effect of the growth in costs will be offset by a decline in firms' profit margins. Inflation will thus stay close to the 2% target over the entire outlook.

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Risks identified by the Scoreboard

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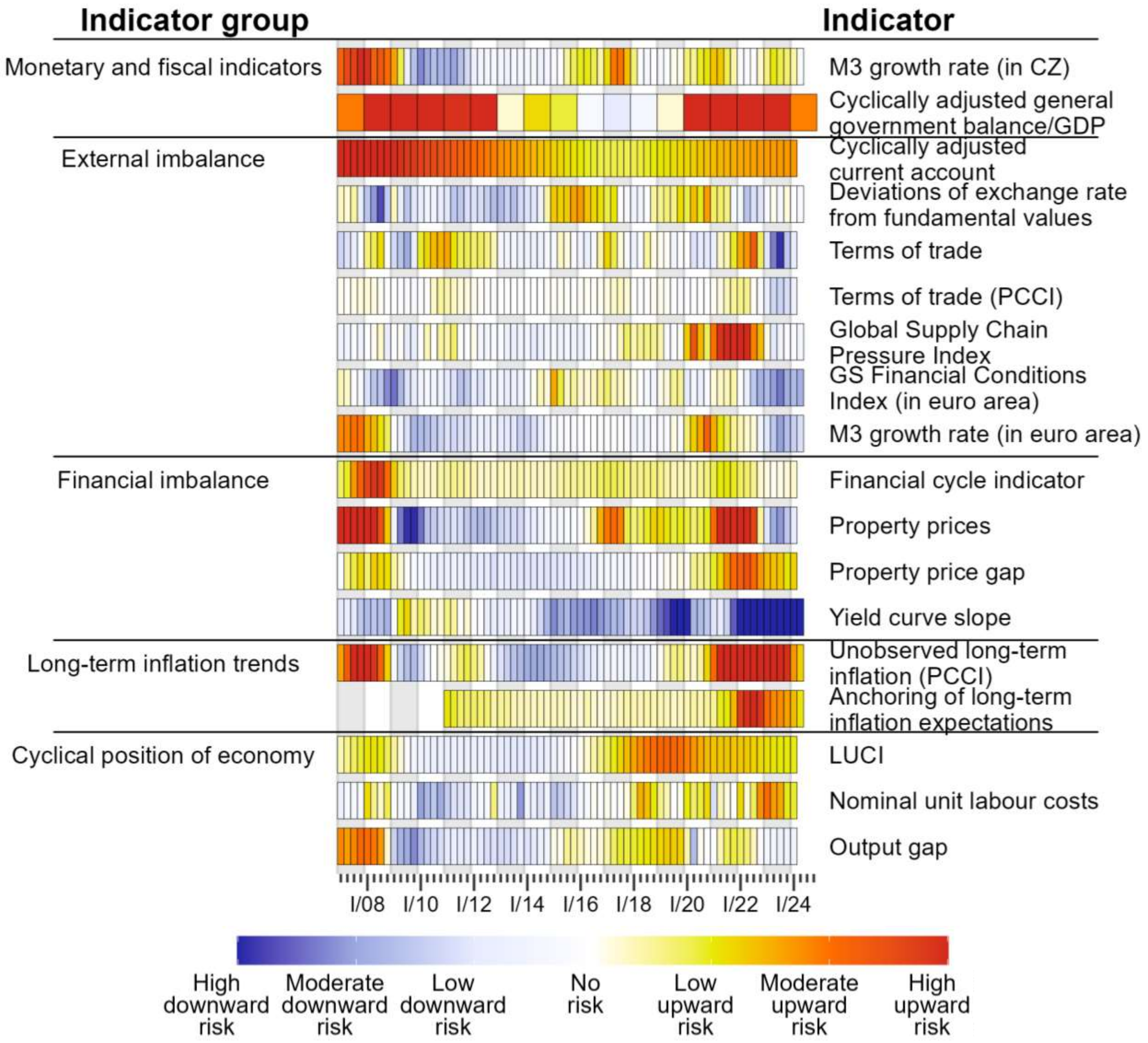
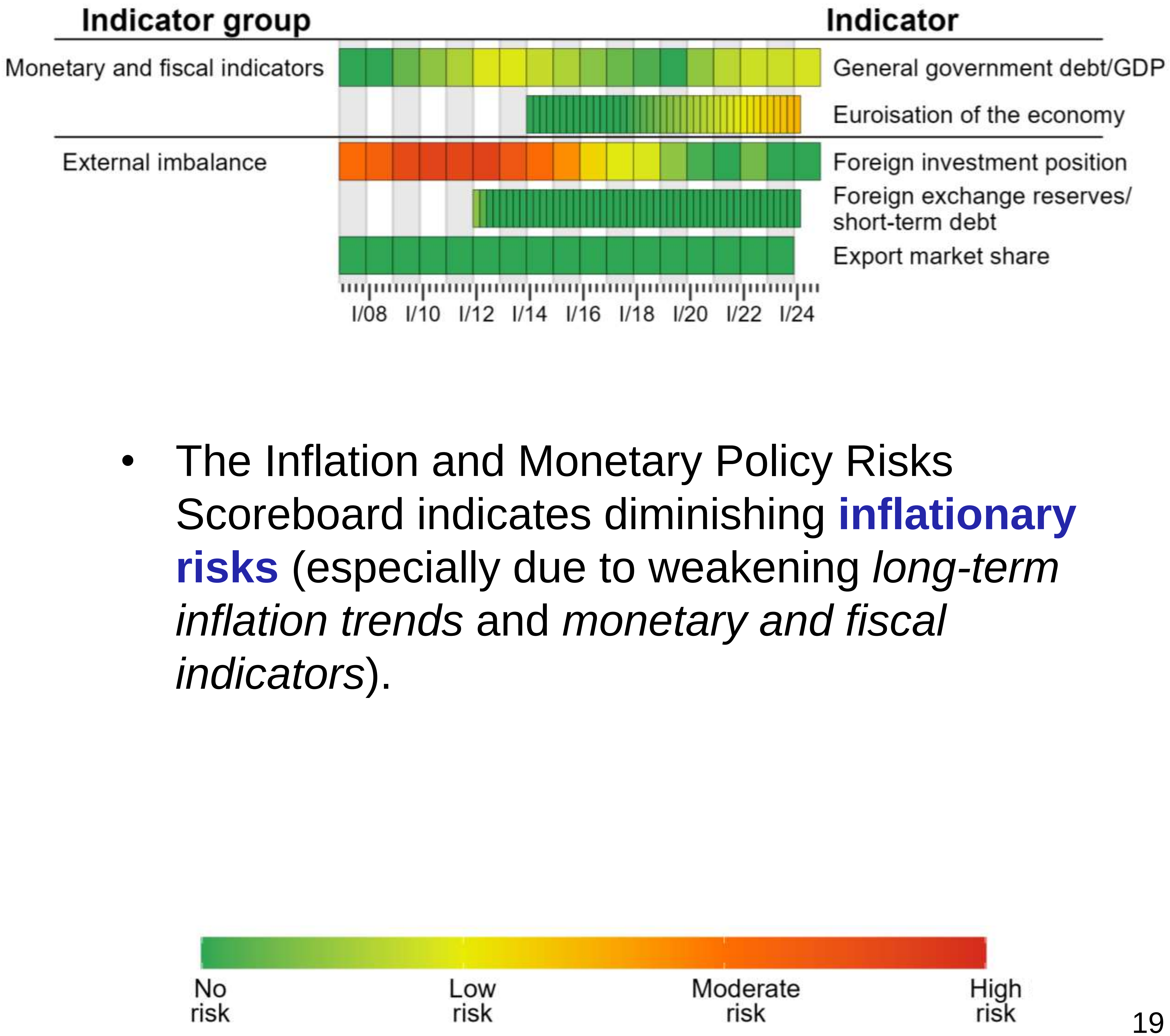
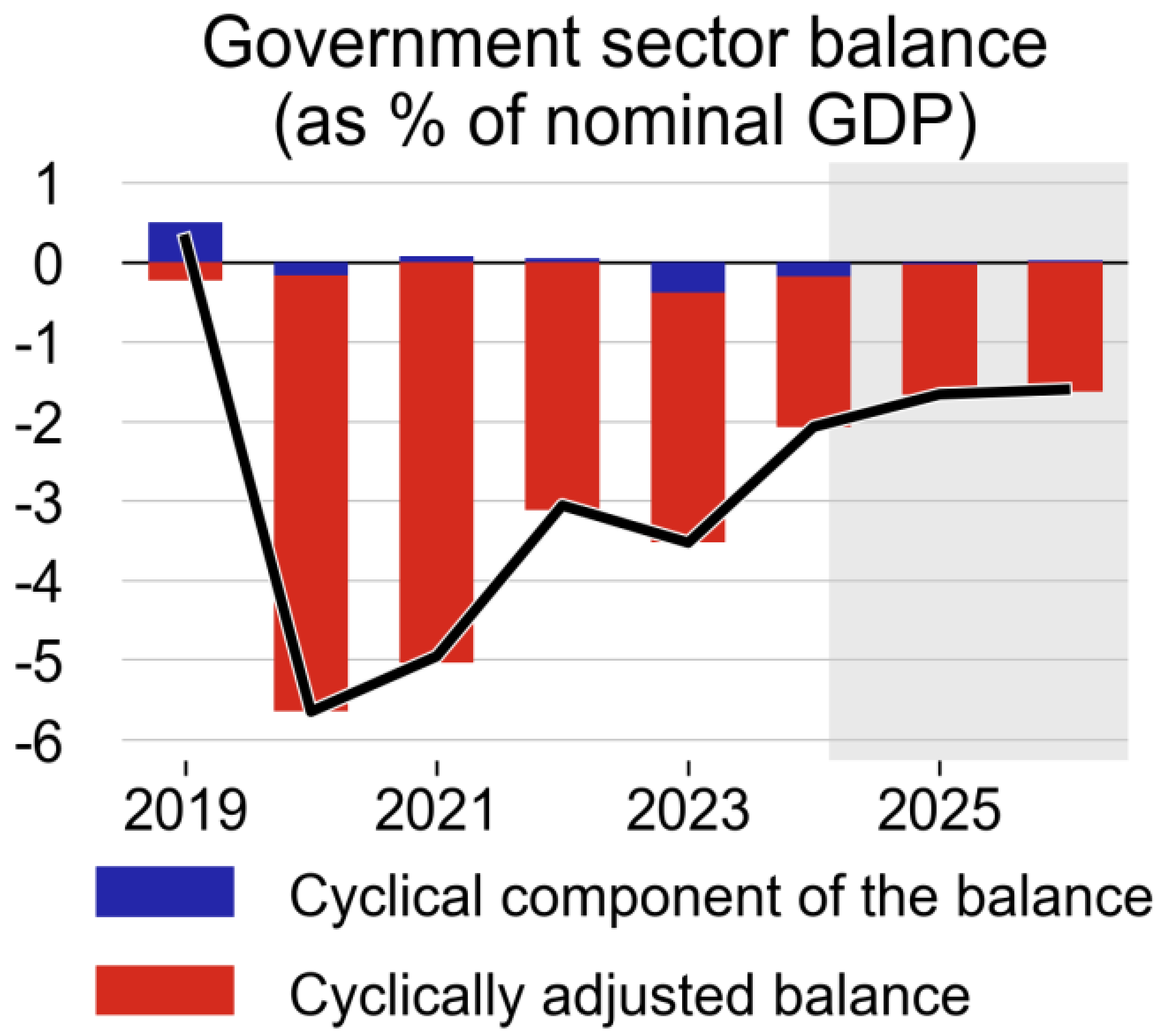
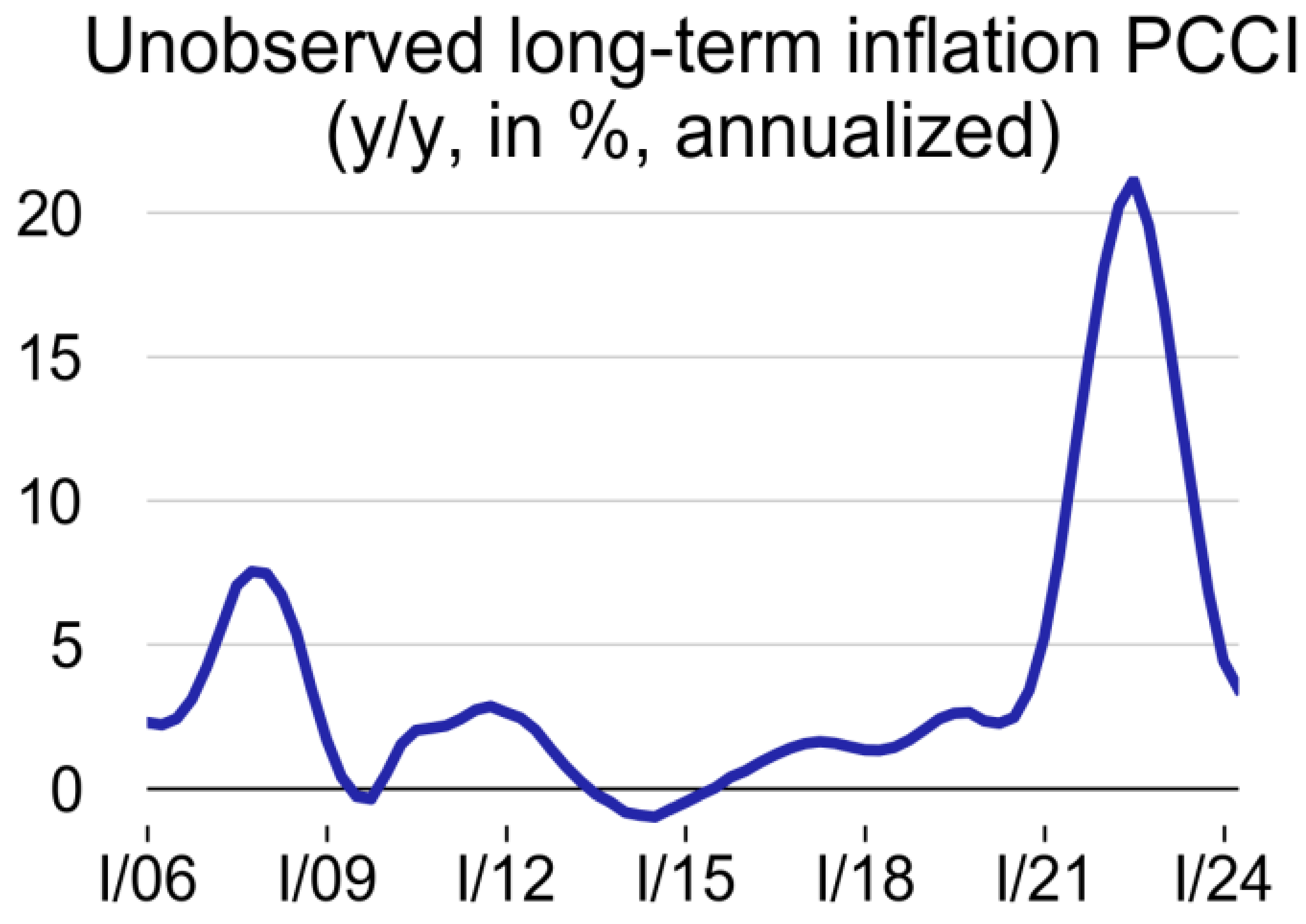


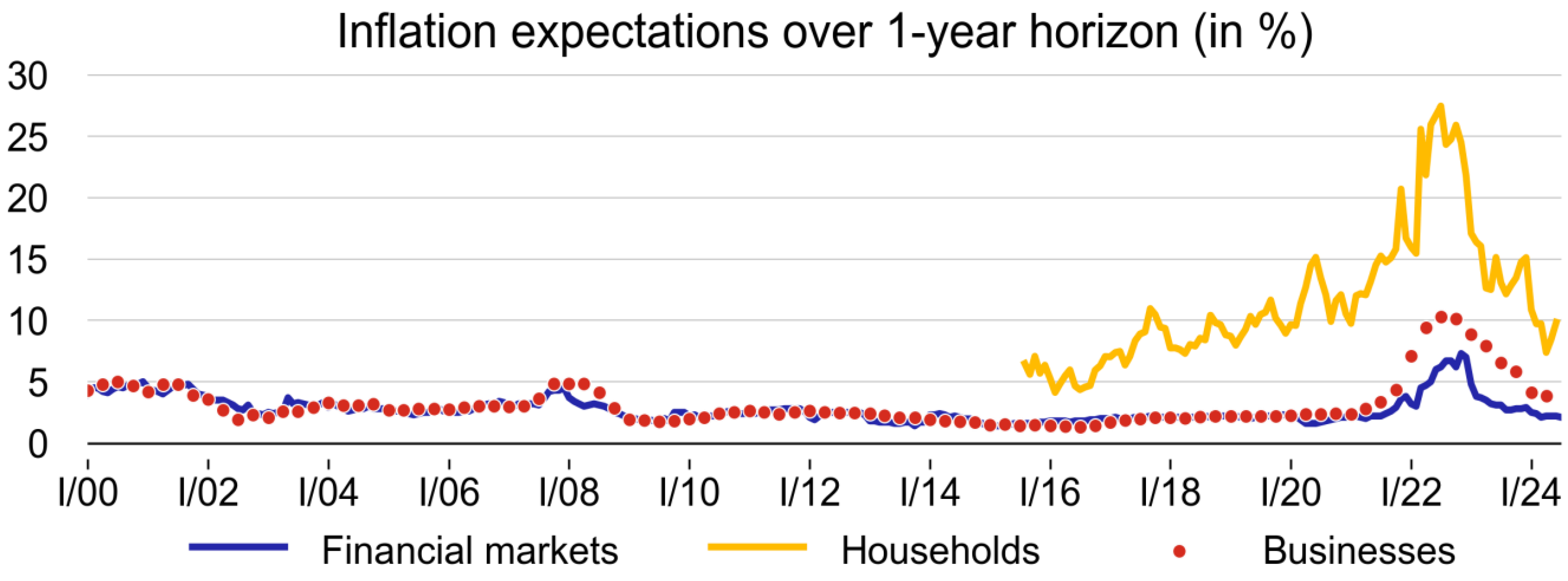


- The Inflation and Monetary Policy Risks Scoreboard indicates diminishing **inflationary risks** (especially due to weakening *long-term inflation trends* and *monetary and fiscal indicators*).

Main Scoreboard Risks







- There is a gradual easing of the inflationary risk related to **government deficit spending** for this year.
- The risk of **long-term inflation** is also gradually weakening.
- **Inflation expectations** have declined but remain well above the 2% target, especially in the case of firms.

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Thank you for your attention.

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Gross Fixed Capital Formation

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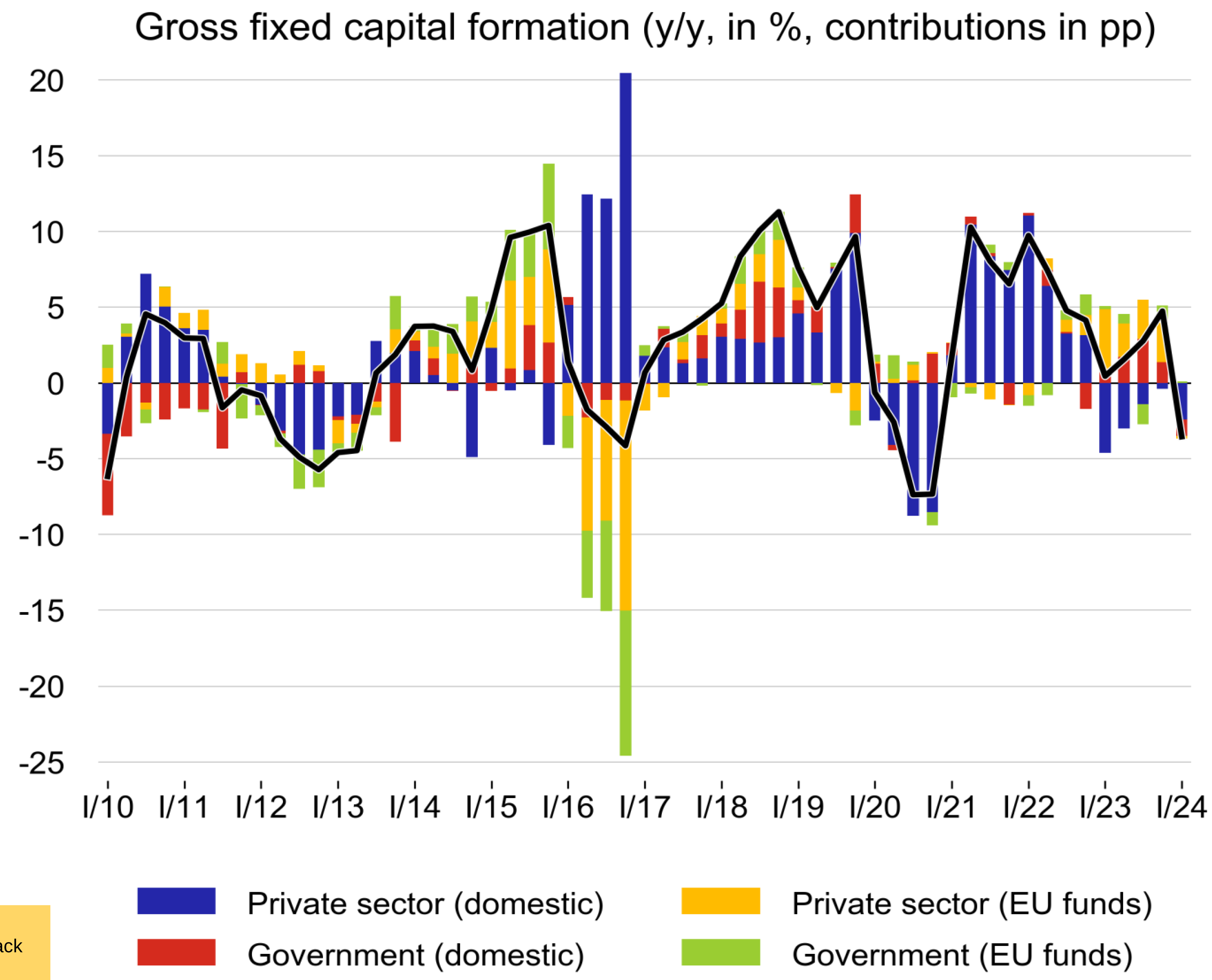

- The growth of **fixed investment** last year was significantly supported by **private sector investment**, which were financed by **EU funds**.
- Private companies utilised approximately CZK 53 billion from EU funds; however, this year, we expect withdrawals of only CZK 25 billion.
- Total investment will slightly decline this year, driven by the shortfall in EU funds that financed private investment last year.
- A similar situation to that of 2015–2016 will occur, although to a lesser extent.
- In contrast, **government investment** financed by EU funds will reach approximately the same level as last year.

Back