
Recent Economic Developments and CNB Monetary Policy

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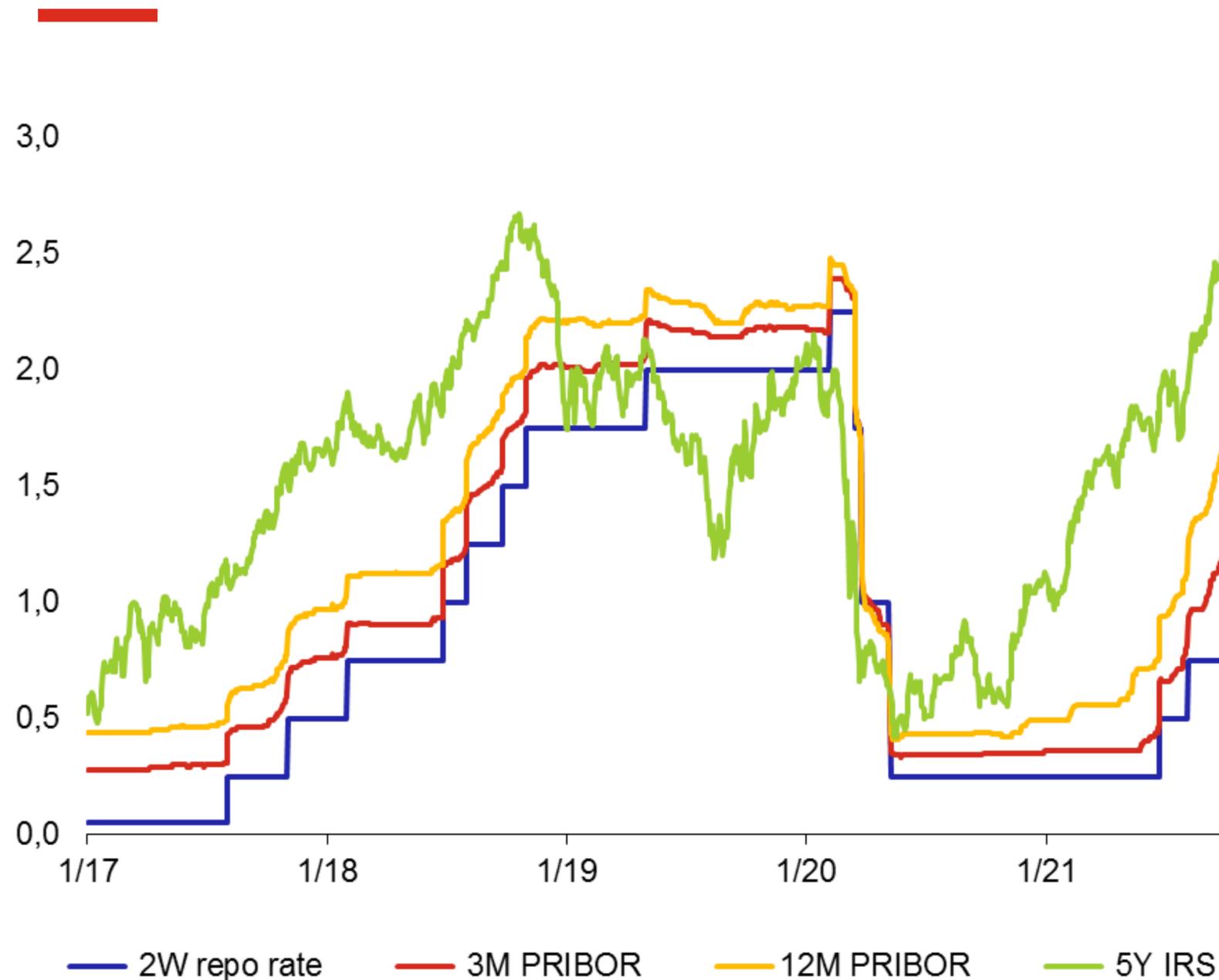
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Covid crisis: basic features and lessons

- Czech economy was overheated when covid crisis struck; it cooled somewhat during crisis, but ongoing recovery is quickly returning it close to pre-crisis level → risk of overheating again is thus rising (especially in labour market)
- Asymmetric impacts of crisis on various sectors have led to flexible structural adjustment of employment and low cyclical growth in unemployment
- Covid crisis has been different to traditional cyclical crises in several respects; past experience with cycle is of limited relevance now; three surprises:
 - Inflation hasn't gone down (unlike in Eurozone)
 - Property market hasn't cooled (as it did during financial crisis) but on the contrary has seen further rapid growth
 - Major disruptions on supply side (which is not recovering as fast as demand) have caused massive growth in cost-push inflation pressures; these are not typical of initial recovery phase

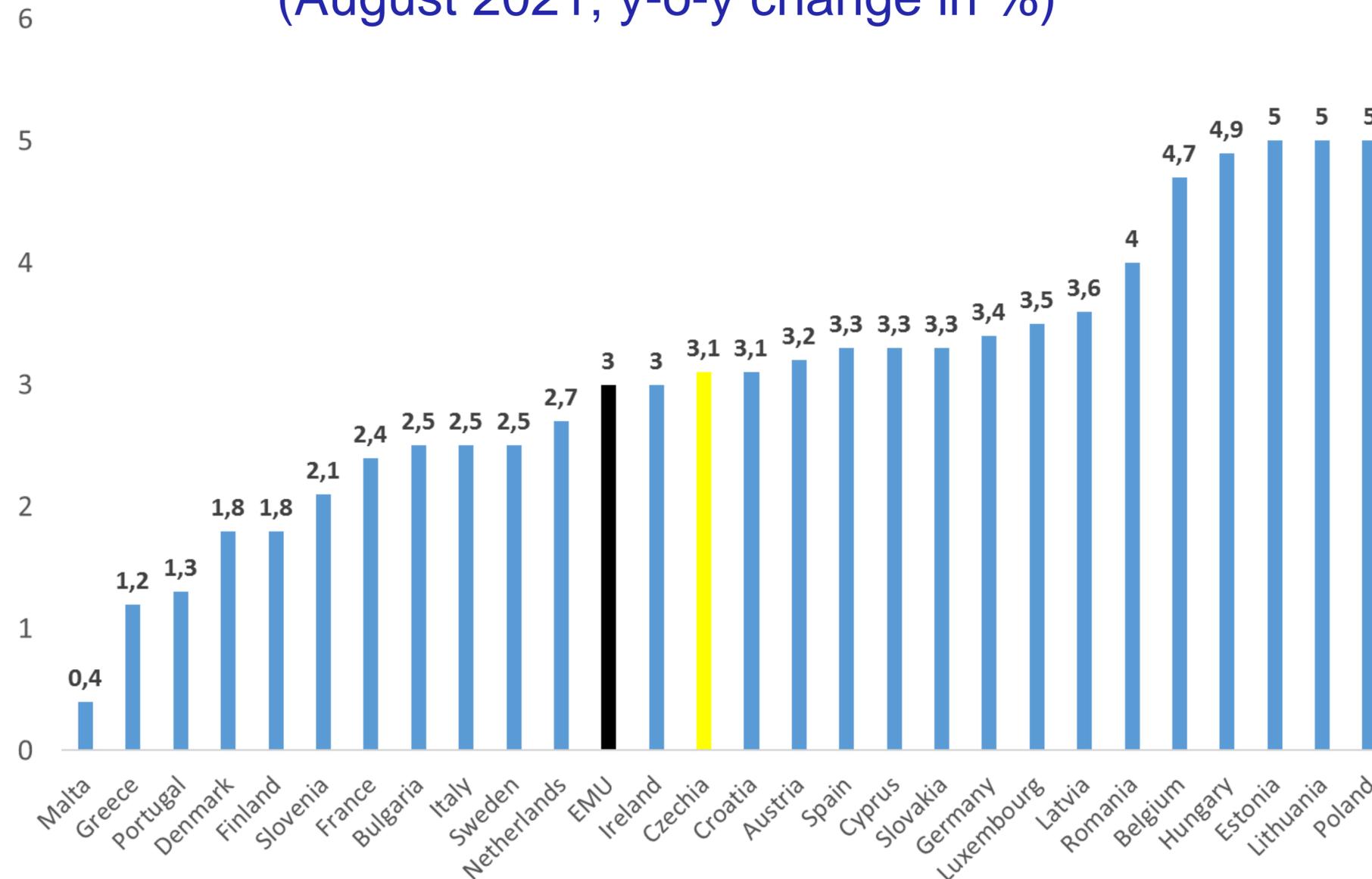
CNB monetary policy during covid crisis: three phases



1. Mar–May 2020: rapid rate reduction of 2 pp in three steps (more intuition than model-based approach)
2. Mid-2020–mid-2021: stable rates (several waves of pandemic and persistent uncertainties)
3. Mid-2021 onwards: normalisation of interest rates (quick withdrawal of lockdowns; diminishing uncertainties); accelerated hike of 0.75 pp in September (enhanced cost risks and ensuing risk of de-anchored inflation expectations)

HICP in European Union

(August 2021; y-o-y change in %)

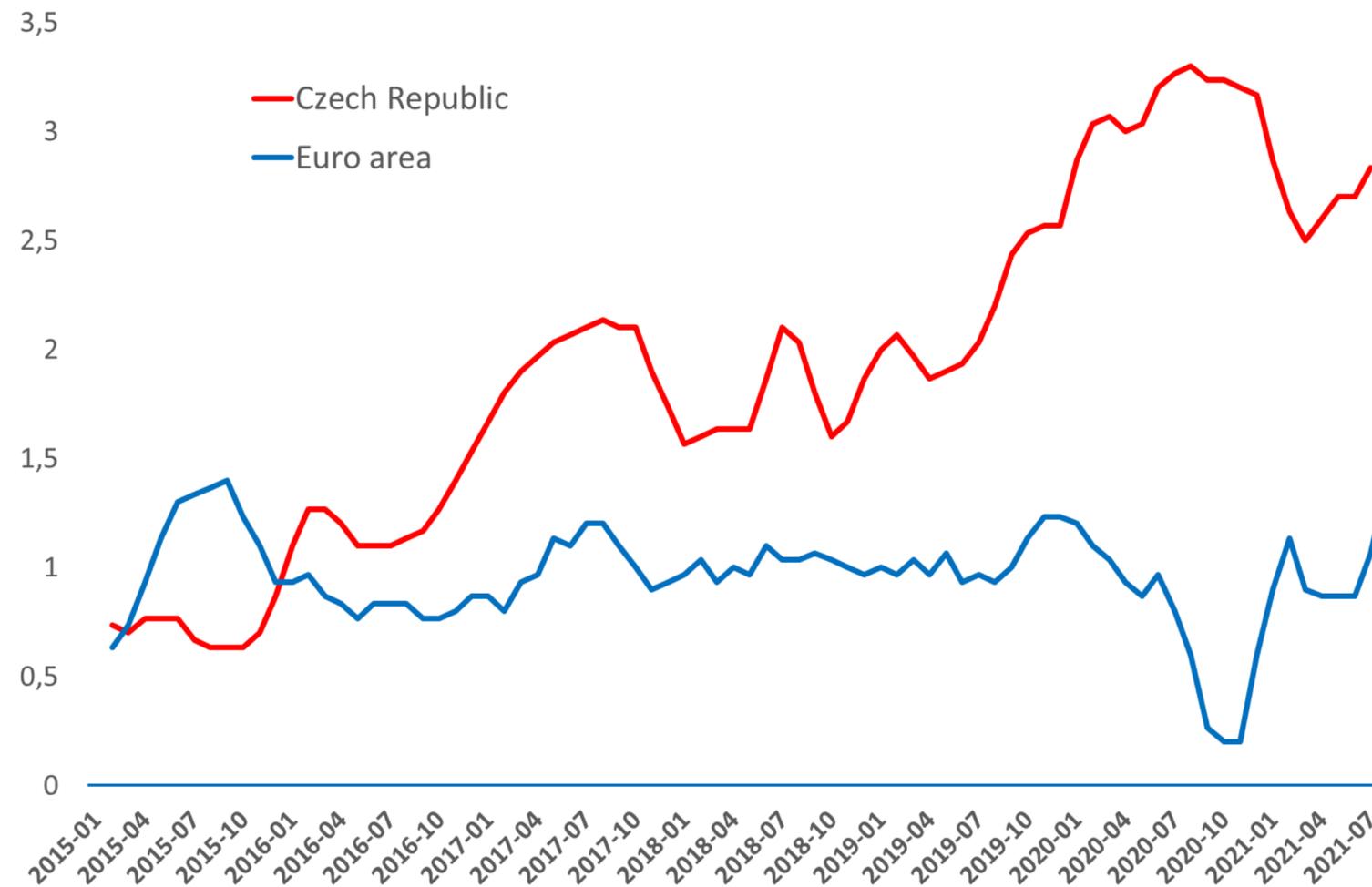


Source: Eurostat,
own computation

Headline HICP inflation in Czech Republic was comparable with that in Eurozone in August 2021...

Core inflation in Czech Republic and euro area

(Jan 2015–Aug 2021; 3-month moving average)



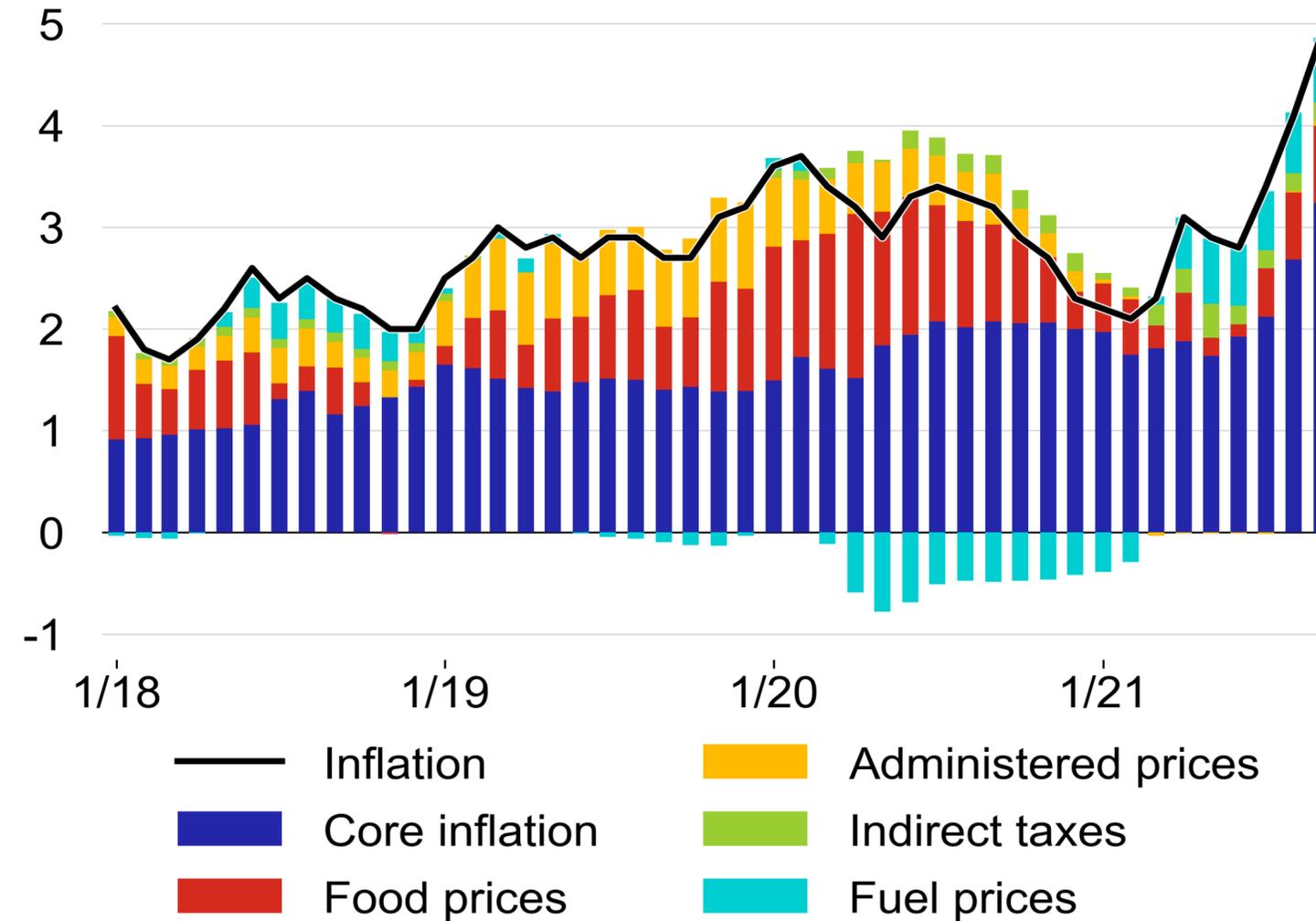
Note: Core inflation = Overall index excluding energy, food, alcohol and tobacco

Source: Eurostat,
own computation

...but core inflation in Czech Republic was and is systematically higher than in Eurozone, putting CNB in different monetary policy situation than ECB

Inflation in Czech Republic in Sep 2021

Inflation decomposition
(YoY, in %)



CPI: 4.9% (CNB August forecast: 3.2%); core inflation: 5.8% (forecast: 3.5%); food: 2.8% (forecast 2.1%); surprise: clearly on upside

Monetary policy challenges for CNB

- CNB is committed to fulfilling its statutory mandate to maintain price stability
- CNB must take into account that Czech economy is in different situation than Eurozone (and was even before crisis)
- Czech Republic has its own currency – this allows it to spread monetary tightening into interest and exchange rate component (import price channel)
- CNB will focus on suppressing second-round inflation pressures and try to prevent wage-price spiral
- CNB will act in forward-looking fashion:
 - to keep inflation expectations anchored at inflation target
 - to maintain credibility of inflation target and of its monetary policy

Future risks and uncertainties

- Disruptions to global production and supply chains: intensity and duration of cost shocks
- Intensity of long-term cost pressures associated with EU environmental policies (electric cars, Green Deal, carbon neutrality, etc.)
- Degree of pass-through of cost pressures to inflation
- Strength of anchoring of inflation expectations amid sustained overshooting of inflation target
- Speed and intensity of future fiscal consolidation
- Overall balance of risks: on upside



Thank you

