

# Macro Monitor

## Czech Republic

- In the following pages we present an updated outlook on the Czech economy, taking into account the latest economic releases for August and September.
- The Czech economy has been hard hit due to the recession in western Europe as foreign demand for Czech exports plunged and investments suffered badly during the crisis. Economic activity dropped significantly in Q1 and Q2 this year, but it looks very likely that the economic contraction has reached the bottom and that we should see the economy recovering in coming quarters, albeit very gradually. We expect GDP to contract on average by 4.4% y/y in 2009 and grow 0.1% y/y in 2010.
- The signs of recovery in the eurozone will have a positive impact on exports and production in the Czech Republic. Exports have already begun moving up and industrial production should improve by the end of the year. This will consequently affect investments, which are expected to gradually recover, but in H1 10 at the earliest. We expect private consumption to begin moving up but here we see downside risk to our forecast as fiscal measures approved by the government in order to cut the next year's budget deficit will likely have a negative impact on consumption. Labour market conditions will continue to deteriorate with rising unemployment well into 2012.
- Above mentioned fiscal measures create considerable uncertainty to our 2010 GDP forecast and clearly represent downside risk to our forecasts.

### Macro forecast

Year	Gdp(1)	Private. cons(1)	Fixed Inv(1)	Export(1), (4)	Import(1), (4)	Trade Balance(2), (4)
2008	2.6	3.4	-1.0	0.2	1.0	2.1
2009	-4.4	1.5	-8.2	-14.9	-19.4	5.1
2010	0.1	1.0	-1.0	4.2	1.8	6.4
2011	2.8	2.4	3.7	13.0	13.5	6.8

1) Average %/y 2) % of GDP 3) % of total work force 4) Export and import prices, EUR

Source: Reuters Ecowin and Danske Markets

### Macro forecast

Year	Current acc.(2), (4)	Industrial prod.(1)	Unemployment(3)	Wages(1)	Inflation(1)	Retail sales (1)
2008	-4.1	-1.5	5.9	8.4	6.4	-0.4
2009	-1.1	-14.1	9.2	1.9	1.0	-6.2
2010	0.2	1.1	10.7	1.5	0.2	3.1
2011	0.7	6.2	11.6	3.2	0.9	6.7

1) Average %/y 2) % of GDP 3) % of total work force 4) Export and import prices, EUR

Source: Reuters Ecowin and Danske Markets

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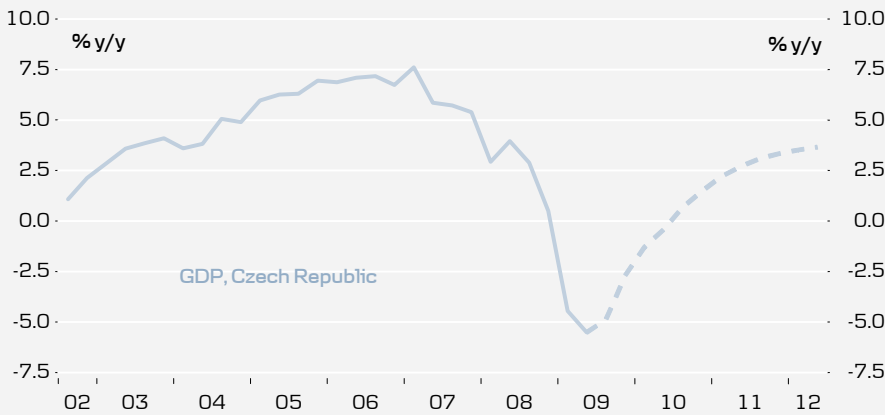
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# Economic growth

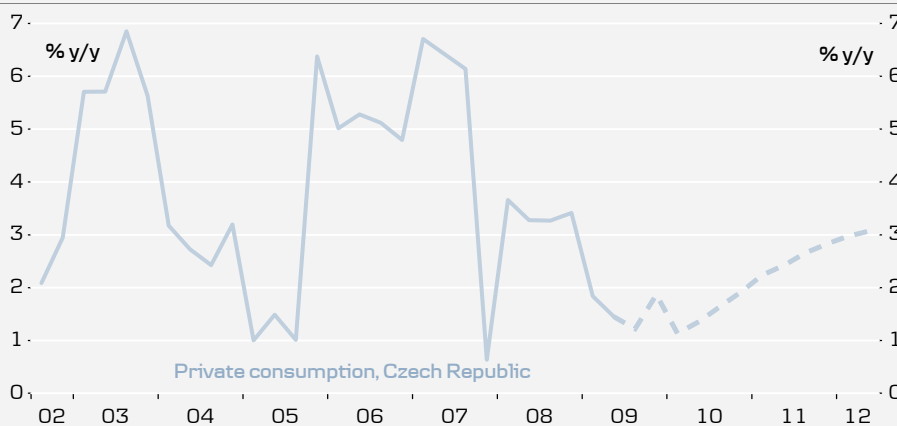
## Gross domestic product



Source: Reuters Ecowin and Danske Markets

- The Czech economy has experienced a significant downturn during the global economic crisis. However, it looks as if the drop in economic activity has reached the bottom and we should see the Czech economy gradually recovering in the coming quarters. We forecast that the Czech economy will contract 4.4% y/y in 2009 and grow 0.1% y/y in 2010.

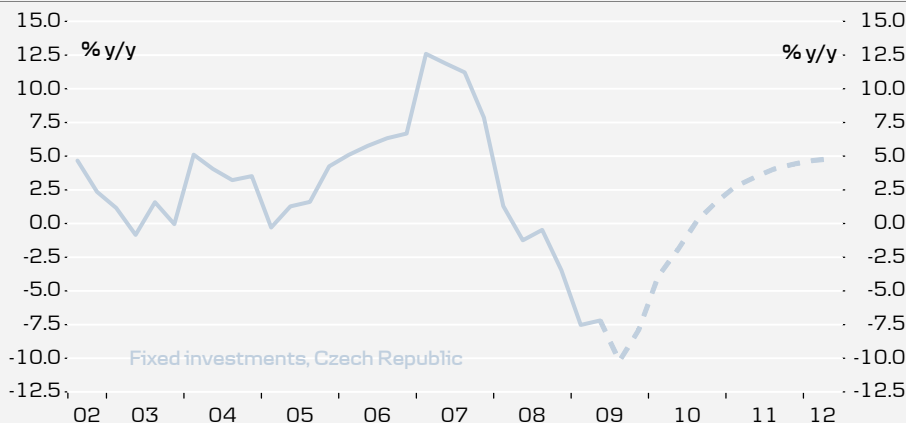
## Private consumption



Source: Reuters Ecowin and Danske Markets

- Czech private consumption has dropped as wage growth has dropped and unemployment has begun rising.
- We expect, however, that private consumption will slowly begin to move up. We predict it to grow on average by 1.5% y/y in 2009 and 1% y/y in 2010. However, the fiscal package clearly represents downside risk.

## Investments

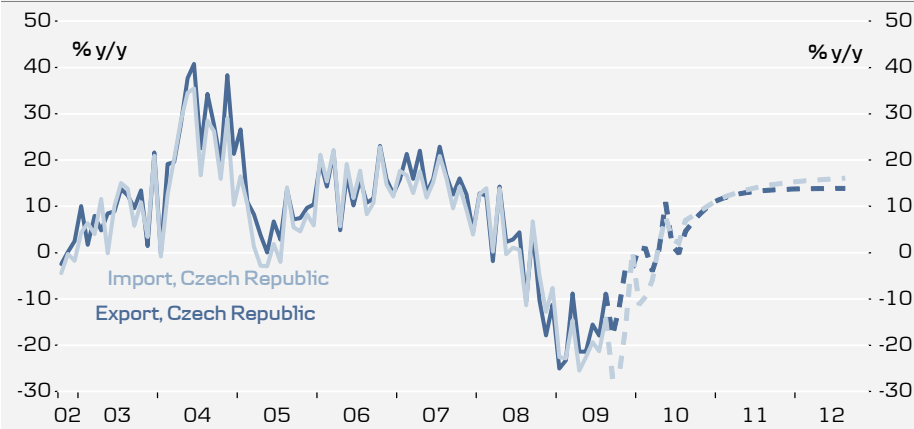


Source: Reuters Ecowin and Danske Markets

- Investments have struggled badly during the crisis and production and exports have weakened and credit conditions have tightened.
- Investments should drop further in Q3 09, after which it will begin to move up. Overall, investments should contract 8.2% y/y in 2009 and 1% y/y in 2010.

# External balances

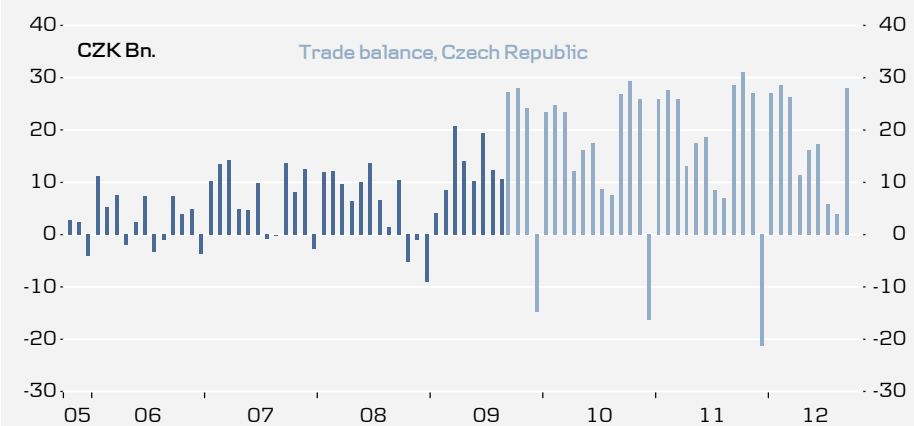
## Exports and imports



Source: Reuters Ecowin and Danske Markets

- Exports have dropped significantly during the economic crisis. However, as signs of recovery are showing in the eurozone, exports have begun moving up. We expect exports to contract 14.9% y/y in 2009 and to grow 4.2% y/y in 2010.
- Imports have also dropped as domestic demand has suffered.

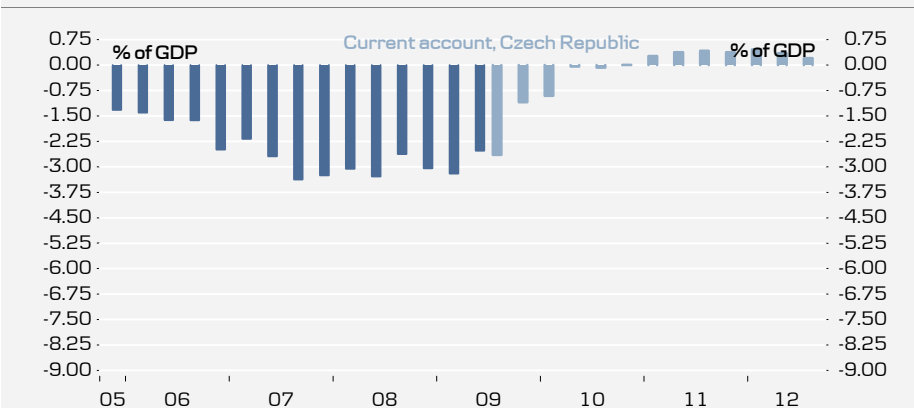
## Trade balance



Source: Reuters Ecowin and Danske Markets

- The Czech trade surplus has expanded during 2009 as imports have suffered worse than exports.
- We expect the trade surplus to grow further in the period ahead, as exports are expected to recover faster than imports. Our forecast is a trade surplus of 5.1% of GDP in 2009 and 6.4% of GDP in 2010.

## Current account

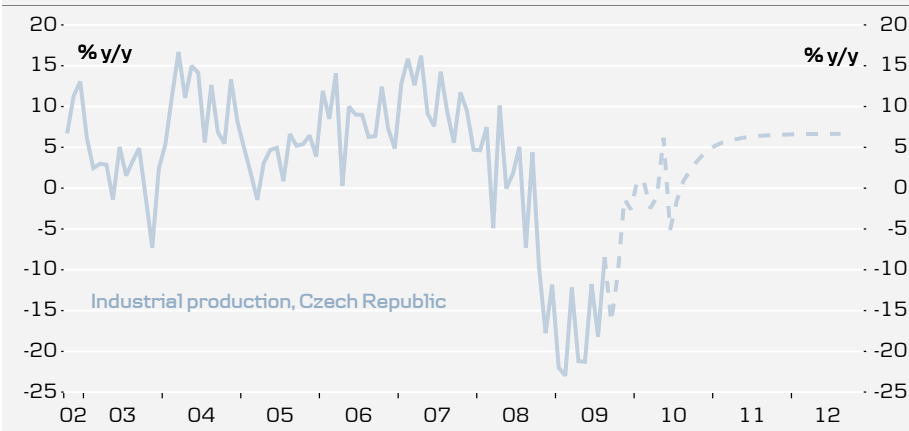


Source: Reuters Ecowin and Danske Markets

- The increasing trade surplus in the Czech Republic will improve the current account situation.
- We expect the Czech current account balance to go to zero in 2010.

# Production and labour market

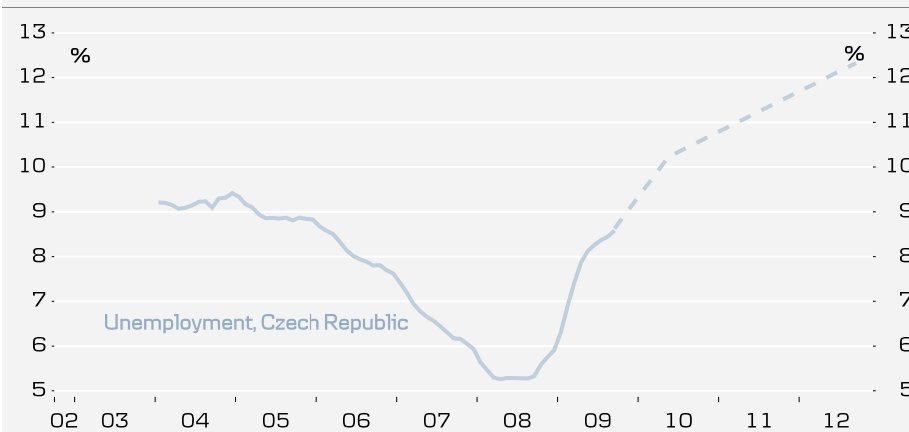
## Industrial production



Source: Reuters Ecowin and Danske Markets

- Czech industrial production was hard hit by the economic crisis as foreign demand for Czech products plunged. Better performance of the Czech industry in Q4 will be helped by a strong base effect. Further recovery depends greatly on the recovery in Europe.
- We expect average industrial production to fall by 14.3% y/y and by 0.4% y/y in 2010.

## Unemployment

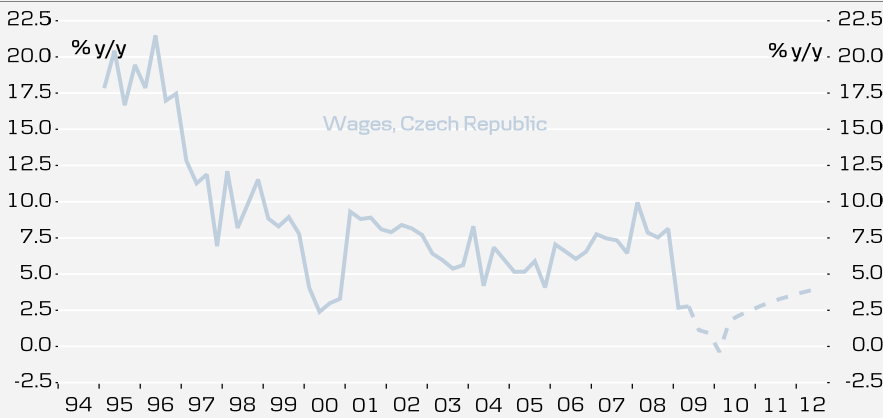


Source: Reuters Ecowin and Danske Markets

- The economic crisis has been accompanied by rising unemployment, which continues creeping up each month.
- Unemployment is expected to rise to 9.2% in 2009 and to 10.7% in 2010.

# Wages, prices and retail sales

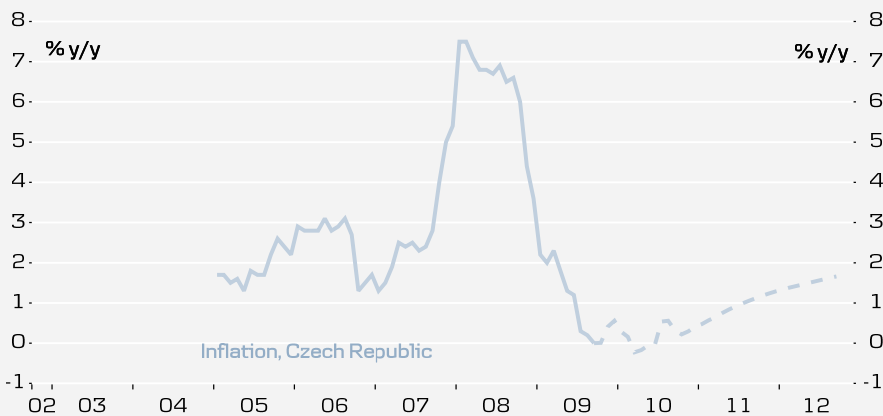
## Wages



Source: Reuters Ecowin and Danske Markets

- The downturn in economic activity and rising unemployment resulted in slowdown in wage growth. We expect further slowdown in wage growth going into 2010.
- We see stabilisation during in Q1 next year and wage growth should start moving up in Q2 next year. On average we expect wage growth at 1.9% y/y in 2009 and 1.5% y/y in 2010.

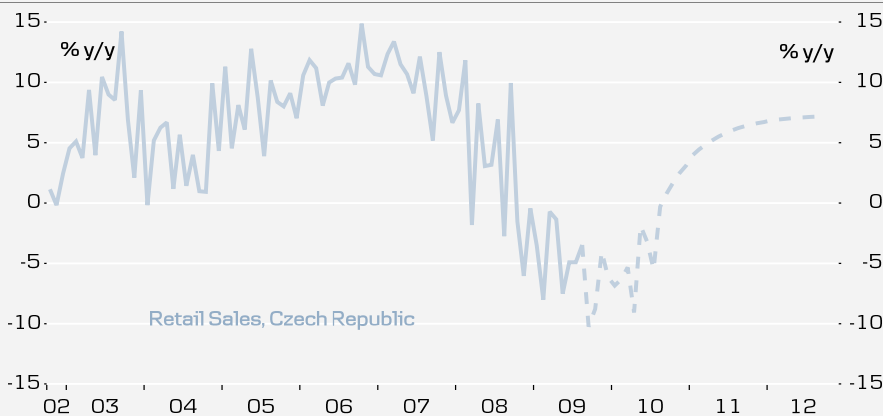
## Inflation



Source: Reuters Ecowin and Danske Markets

- Despite inflation likely to inch up at the end of this year, due to a strong base effect from last year's low oil prices, it will stay at very low levels. On average we expect inflation in 2009 at 1% y/y.
- We expect no real inflationary pressures further into 2010. Some upside risks to our average 2010 inflation forecast of 0.2% y/y are due to VAT and other indirect taxes hikes next year.

## Retail sales



Source: Reuters Ecowin and Danske Markets

- Czech retail sales remain weak as rising unemployment and stagnating wages put a lid on consumers spending.
- We expect retail sales to fall further well into 2010. We see retail sales on average at -6.2% y/y in 2009 and 3.1% y/y in 2010.

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All EM research is available on Bloomberg DDEM

## Disclosure

This report has been prepared by Danske Research, which is part of Danske Markets, a division of Danske Bank. Danske Bank is under supervision by the Danish Financial Supervisory Authority. The authors of this report are Stanislava Pravdova, Analyst and Jens Nærvig Pedersen, Assistant Analyst

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