Monetary Policy Report
Autumn 2024

Czech National Bank —— Monetary Policy Report —— Autumn 2024

CZECH NATIONAL BANK

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This Monetary Policy Report was approved by the CNB Bank Board on 14 November 2024 and (with some exceptions) contains the information available as of 31 October 2024. By means of this document, the CNB fulfils its statutory duty to regularly inform constitutional officials and the public about monetary developments. Unless stated otherwise, the sources of the data are the CZSO or the CNB. All the reports published to date, along with the underlying data, are available on our website. A large part of the data we evaluate in our monetary policy decision-making can be found in the Chartbook, which is a parallel publication to the Monetary Policy Report.

Contents

— We maintain price stability

Under the Constitution of the Czech Republic and in accordance with primary EU law, the primary objective of the Czech National Bank is to maintain price stability. The central bank contributes to sustainable economic growth by maintaining a low-inflation environment. We have been pursuing price stability in an inflation-targeting regime since 1998.

— We are transparent

Our monetary policy is based on a publicly announced inflation target of 2% and open communication with the public. We believe that by being transparent and predictable, the central bank assists households and companies in their economic decision-making.

— We look to the future

A decision made by the CNB Bank Board today will affect inflation 12–18 months ahead. The CNB's forecast describes the most likely future path of the economy as seen by our Monetary Department's economists. The Bank Board is continuously informed about the forecast under preparation, discusses the outline of the emerging baseline scenario and asks for potential additional forecasting scenarios to be drawn up. The forecast is produced four times a year and, along with a discussion of related risks and uncertainties, is the key, but not the only, input to the CNB Bank Board's monetary policy decisions.

— We decide on rates

The CNB's main monetary policy instrument is the two-week repo rate. The decision on the level of this rate sends an impulse through the financial market to the whole economy, ultimately affecting inflation in such a way as to keep it close to the target. The Bank Board meets eight times a year to discuss monetary policy issues. When making rate decisions, the members of the Bank Board discuss the current forecast and assess the newly available information and the risks and uncertainties of the forecast.

Governor's foreword

Dear Readers,

It is my pleasure to present the autumn Monetary Policy Report. The Report is one of the main inputs to the Bank Board's decision-making on CNB monetary policy.

At our November meeting, my Bank Board colleagues and I lowered the two-week repo rate by 0.25 percentage point to 4%. We also lowered the other key interest rates by the same amount. This was our eighth cautious easing of monetary policy since last December. Monetary policy nonetheless remains tight. Real interest rates are positive and are dampening lending activity, and hence the creation of money in the economy, and, in turn, long-term inflation.

Inflation has been close to the 2% target since the beginning of this year. Price stability has thus been restored. We expect inflation to rise temporarily in the short term, i.e. over the next few months, owing to renewed growth in food prices. In addition, core inflation remains elevated, especially in services. Therefore, the Bank Board will approach future monetary policy easing with great caution and may pause the interest rate reduction process.

The Monetary Department's new forecast, which is described in detail in this Report, implies a modest decline in interest rates. The Bank Board also discussed two alternative scenarios. The first one assumes a further downturn in euro area economic activity, reflected in lower external demand and a faster decline in domestic inflation towards the target. The second scenario assumes higher retailers' margins than in the baseline scenario. This would lead to greater persistence of inflation, especially in the services sector.

The use of alternative scenarios as a tool for communicating the risks associated with the forecast is one of the conclusions of the review of the CNB's modelling framework published on the CNB website on 11 November. I expect us to continue to use alternative scenarios more often than in the past. This will allow us to better communicate the scenarios we consider and any deviations of monetary policy from the baseline scenario. We will gradually implement the conclusions of the monetary policy review and are currently discussing the relative priorities of the recommendations.

To conclude this foreword, I would like to assure the public on behalf of the Bank Board that the CNB's actions will be sufficient to maintain price stability in accordance with its statutory mandate. In addition, the Bank Board is ready to react appropriately to any materialisation of the risks of the forecast.

On behalf of the Czech National Bank

Aleš Michl

Governor

The decision, the outlook and associated risks

At its November meeting, the Bank Board lowered the two-week repo rate by 0.25 pp to 4%. Inflation has been close to the 2% inflation target for most of this year. However, it increased to 2.6% in September and will rise just above 3% temporarily at the turn of the year. This acceleration is due mainly to food prices, whose renewed growth will strengthen further in the months ahead. By contrast, core inflation adjusted for volatile food items, energy and administrative effects remains slightly above 2%, reflecting a slow unwinding of the downturn in demand in the domestic economy and abroad. Inflation will start to fall again gradually at the start of 2025 and stabilise close to the target in 2026, owing to lower growth in administered prices and later also food prices. Economic growth is recovering gradually, aided not only by household consumption amid renewed growth in real wages, but also by general government consumption. Inventories and subdued external demand are having the opposite effect. Economic growth will rise to 2.4% next year, driven by renewed investment growth, a further strengthening of household consumption and a recovery in our main trading partner countries. Consistent with the autumn forecast is a continued decline in short-term market interest rates initially, followed by broadly stable rates from mid-2025 onwards. A still tight interest rate stance will support the stabilisation of inflation close to the target over the monetary policy horizon. However, the need for monetary policy restriction will decrease as inflation pressures ease. The Bank Board assessed the risks and uncertainties of the outlook for the fulfilment of the inflation target as modestly inflationary overall.

Inflation has been exactly at, or close to, the CNB's 2% target this year. In recent months, however, it has recorded slight growth, which will continue at the year-end. Inflation will briefly rise slightly above the upper boundary of the tolerance band around the target at the turn of the year, on the back of renewed growth in prices of food, beverages and tobacco, which will rise further over the next few months. In year-on-year terms, this will be due not only to the fact that food prices were falling this time last year, but also to the gradual pass-through of higher prices of some food commodities.

By contrast, administered price inflation will slow sharply to less than 2% next year. The announced reduction in the commodity component of housing-related energy prices will be offset by an increase in other items, such as licence fees. Fuel prices will continue to decline year on year this year and the next.

By contrast, core inflation is stable slightly above 2% and will stay close to this level in the coming years. This reflects not only fading cost pressures, but also subdued demand in the Czech economy, which is manifesting itself in a decrease in the until recently highly elevated profit margins.

Within core inflation, services prices are rising more quickly than goods prices. Persistent elevated growth in prices of market services is making headline inflation more susceptible to shocks in volatile items, as illustrated by the renewed food price inflation in recent months. A scenario considering a slower decline in profit margins, implying faster-than-forecasted growth in services prices, has therefore been constructed. The scenario leads to higher inflation next year despite tighter monetary policy in the form of higher interest rates.

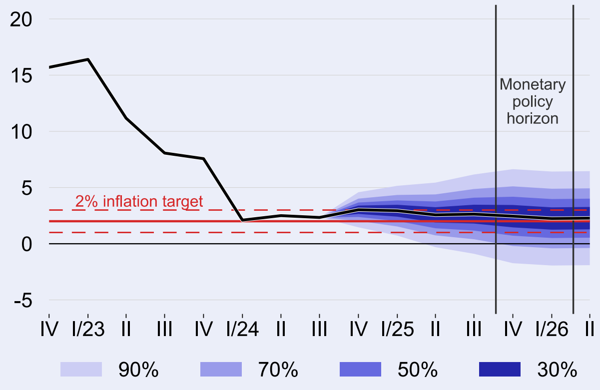
Another risk of the forecast – a higher-than-expected recovery in demand on the housing and mortgage markets – is also linked with prices. Further growth in demand for mortgage loans would mean additional money creation and create an environment for the emergence of disequilibria in the economy. This risk is discussed in detail in the Appendix.

The economy has started to grow again this year. The recovery is being driven by household consumption, although its growth is weak compared with the solid growth in real income. This is because the saving rate remains significantly above average, with saving still being motivated by elevated real interest rates in addition to weak consumer confidence. As a result, household consumption will grow at a solid pace next year. It will be supported by still low unemployment and continued solid nominal wage growth, which, however, will be lower than in the previous two years.

Investment activity has been subdued so far this year. It mainly reflects a negative contribution of additions to inventories, with the level of inventories even falling. This is due to renewed smooth functioning of supply chains, which has enabled firms to complete

Inflation will be close to the upper boundary of the tolerance band around the target at the turn of the year and will then start to decline gradually towards the 2% target

headline inflation; y-o-y in %; confidence intervals in colours



The Czech economy is returning to growth this year and will accelerate to 2.4% in the next two years

y-o-y changes in % (unless otherwise indicated); changes in pp compared to previous forecast in brackets

	2024	2025	2026
Headline inflation (%)	**2.5**	**2.6**	**2.2**
	(0.2)	(0.7)	(0.2)
GDP	**1.0**	**2.4**	**2.4**
	(-0.2)	(-0.3)	(0.1)
Average nominal wage	**6.4**	**5.7**	**5.1**
	(-1.0)	(-0.7)	(-0.1)
3M PRIBOR (%)	**4.9**	**3.2**	**3.0**
	(-0.2)	(-0.7)	(-0.3)
Exchange rate (CZK/EUR)	**25.1**	**25.4**	**25.5**
	(0.0)	(0.5)	(0.8)

Green indicates a shift of the forecast to higher levels, or to a weaker koruna exchange rate, compared with the previous forecast. Red indicates a shift in the opposite direction.

and export their unfinished products and is no longer forcing them to hold excessive stocks of inputs. Growth in fixed investment will also pick up as external demand gradually recovers and interest rates continue to fall in the domestic economy and abroad. By contrast, net exports of goods and services will make a negative contribution to economic growth as import-intensive investment and consumption rise.

General government consumption is continuing to rise strongly this year but will slow in the coming years. The government's consolidation efforts are reflected in a restrictive fiscal impulse this year. This is visible most of all in a decrease in household consumption and reduces GDP growth by 0.7 pp. Next year, government measures will have a broadly neutral effect on economic growth.

External demand will recover only very slowly. Moreover, even this modest recovery is not risk-free. An escalation of the problems in German industry would adversely affect other EU economies, including the Czech Republic. This risk is quantified in another scenario, which involves continued stagnation of the German economy with spillovers to other countries, coupled with disinflationary tendencies and a faster decrease in ECB rates in line with their current market outlook. The scenario is therefore in many respects close to the current view of the financial markets, which, however, often tend to be overly pessimistic. For the Czech economy, the scenario implies markedly slower economic growth, especially next year, lower inflation pressures and a deeper decline in interest rates to below their long-run neutral level.

By contrast, the baseline scenario of the forecast assumes a slower decrease in the ECB's rates next year, in line with its communications so far. This expected cautious approach will reflect an increase in euro area inflation at the turn of the year and persisting elevated growth in services prices, like in the domestic economy.

These overall developments are consistent with a slight weakening of the exchange rate. According to the forecast, the rate will be around CZK 25.50 to the euro on average over the next two years. This reflects a very slow recovery of external demand, muted domestic productivity growth and a narrowing interest rate differential vis-à-vis the euro area. The equilibrium rate of appreciation of the koruna has also been reduced starting with the summer forecast.

Consistent with the autumn forecast is a continued decline in short-term market interest rates initially, followed by broadly stable rates from mid-2025 onwards. Despite the decline in rates, their effect – with regard to inflation and inflation expectations – will remain restrictive until the start of next year and support fulfilment of the inflation target over the monetary policy horizon.

The Bank Board assessed the risks and uncertainties of the outlook for the fulfilment of the inflation target as modestly inflationary overall. Higher-than-expected inertia in services inflation is an inflationary risk. Potential excessive growth in total public sector spending would lead to a risk of the state budget having an inflationary effect. Increased wage demands in the private and public sector are an additional upside risk. An inflationary risk in the longer term is a potential acceleration of money creation in the economy stemming from a significant recovery in lending activity, especially on the property market. By contrast, a downturn in global economic activity and weaker German – and hence Czech – economic output are a significant downside risk to inflation. This is also reflected in the outlook for further rate cuts by major central banks.

Steady-state values in the CNB forecast

Starting with the Summer 2024 MPR, the values of long-term potential output growth and other related variables, including the real equilibrium exchange rate appreciation of the koruna, are lower in the forecast. The reasons for the changes were described in detail in the Appendix to the Summer 2024 MPR The slowdown in the long-term potential growth of the Czech economy. In the summer forecast, the changes were made by means of expert adjustments. In the Autumn 2024 MPR, the steady-state values themselves are recalibrated in the g3+ core forecasting model. The following table shows the steady-state annual growth rates of the variables concerned compared to the previous assumptions.

	Earlier equilibrium	New equilibrium
GDP (including domestic components)	3.0%	2.5%
Productivity	3.0%	2.5%
Nominal wage growth	5.0%	4.5%
Appreciation of the CZK/EUR exchange rate	1.5%	1.0%

I. ECONOMIC DEVELOPMENTS ABROAD

Economic growth in the effective euro area remains subdued and should recover gradually in the course of next year. The growth in households' real income has yet to be reflected in their consumption, mainly because of persisting pessimistic sentiment. Industry is being hampered by elevated energy prices and a related loss of competitiveness. Growth in economic activity is being driven by services. Robust demand for services coupled with still high wage growth is fostering persistent higher inflation in this sector. However, this will recede gradually and headline inflation will slow in parallel. The decline in inflation will be aided by the previous decrease in core industrial producer price inflation, which remains muted. Decreasing consumer price inflation will allow the ECB to continue easing monetary policy, which will support corporate investment activity.

Global economic growth is still being driven mainly by large Asian countries

Economic growth slowed visibly in the largest Asian economies in 2024 Q2 and is expected to weaken slightly in China next year, too (see Table I.1). Global industry was recovering promisingly in the first half of this year, but the favourable trend reversed in Q3. PMI leading indicators suggest that the situation in industry will worsen further at the end of the year. Services are showing only a slight slowdown so far. However, the decrease in inflation is expected to continue, due partly to a cooling of the labour markets in most economies. In most countries, though, real household income and consumption expenditure will keep rising. Economic activity will also be supported by further monetary policy easing by major central banks. Heightened geopolitical tensions, especially in the Middle East and Eastern Europe, remain a risk going forward.

The USA is still maintaining the strongest economic growth among large advanced economies. However, it, too, is expected to slow next year. This is confirmed by worse business sentiment regarding the expected situation one year ahead, due to the current political uncertainty. US industry is also showing lacklustre growth, so economic growth is being driven solely by consumer spending on services. Core inflation will ease further this year and the next, allowing the Fed to cut interest rates further, albeit cautiously.

The Chinese economy is still grappling with problems in the property sector and weak domestic demand, while exports remain solid despite new import tariffs in the USA and the EU. The government has announced new monetary policy measures to support lending, aimed at increasing domestic demand. However, it has not yet been detailed how the promised fiscal stimulus measures will be specifically used to support domestic demand. This is undermining investors' confidence and the growth outlook. Export-oriented industry is faring well, while construction-related output is still falling rapidly. Industrial producer prices are going down and consumer prices are on the cusp of deflation.

Table I.1

Economic growth will weaken in the USA and China next year

real GDP; y-o-y changes in %; source: Oxford Economics

	2023	2024 Q1	2024 Q2	2024	2025	2026
Euro area	0.5	0.5	0.6	0.8	1.2	1.5
USA	2.9	2.9	3.0	2.7	2.5	2.5
United Kingdom	0.3	0.3	0.7	1.0	1.5	1.6
China	5.2	5.3	4.7	4.8	4.1	4.0
India	7.8	7.8	6.7	6.8	7.0	6.8

GDP growth in the effective euro area remains subdued, as industrial activity is continuing to decline and household consumption is low despite rising real wages

Economic activity in the effective euro area recorded very weak growth in 2024 H1 (see Chart I.1).[1] The main reason was still cautious behaviour of households, which are maintaining an elevated saving rate despite rising real income. Low household confidence is also playing a role (see Chart I.2). The trends in the euro area as regards the performance of the individual sectors are mixed. Industry is in crisis, not only because of weak global demand, but also due to low competitiveness stemming from higher energy prices and low innovation. By contrast, services are driving the growth of the euro area economy. However, PMI leading indicators suggest a gradual slowdown in this sector as well (see Chart I.3). The labour market remains relatively stable, with the unemployment rate at an all-time low (6.4% in August). Nevertheless, PMI employment indicators point to a cooling of the market and a gradual decline in employment in industry. However, there are significant differences across countries: the labour market is cooling in Germany and France, but unemployment is falling in Spain. The effect of the ECB's tight monetary policy and heightened political uncertainty are keeping corporate investment low, but the decline in interest rates in Q3 has fostered a slight increase in the volume of loans. Lending and investment should thus continue to rise.

The German economy is still facing problems,[2] although the probability of it entering a technical recession in Q3 has decreased due to encouraging growth in retail sales during the summer. Industrial production was highly volatile in Q3 owing to shifts in the timing of company holidays. Uneven developments in new orders are increasing future uncertainty. The number of insolvencies, which is very high by historical standards, has also been rising steadily this year. The unfavourable expected income and economic situation has caused consumer sentiment to worsen. Germany has still not resolved its structural problems, and the medium-term outlook for its economy points to continuing lacklustre performance. The risk of a more pronounced economic downturn in Germany and, in turn, the euro area as a whole, is the subject of a scenario in section IV.

Austria is not faring well either. Its economy will contract this year. Our southern neighbours have long

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1 Effective euro area GDP rose only negligibly quarter on quarter and by 0.5% year on year in 2024 Q2.

2 Many German firms are facing weakening demand amid strong upward pressure on wages and persisting high energy prices. For example, the largest European car maker Volkswagen is considering a number of cost-saving measures, ranging from wage cuts to large-scale lay-offs and plant closures.

Chart I.1

GDP growth in the effective euro area will recover gradually

annual GDP growth in %; contributions in pp; seasonally adjusted

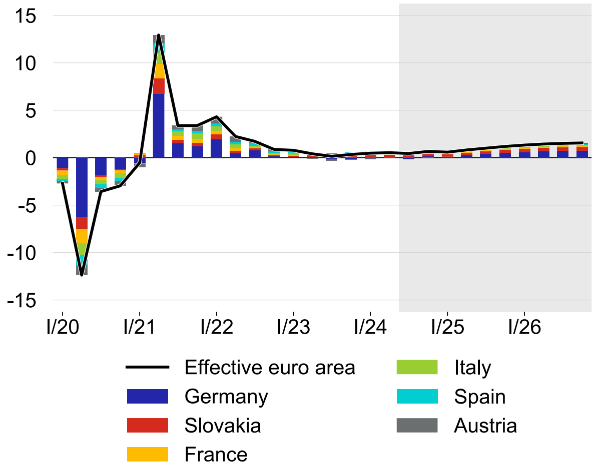


Chart I.2

Consumer confidence in most euro area countries has been broadly flat in recent months

consumer confidence indicators; weighted balance of answers; seasonally adjusted; source: European Commission

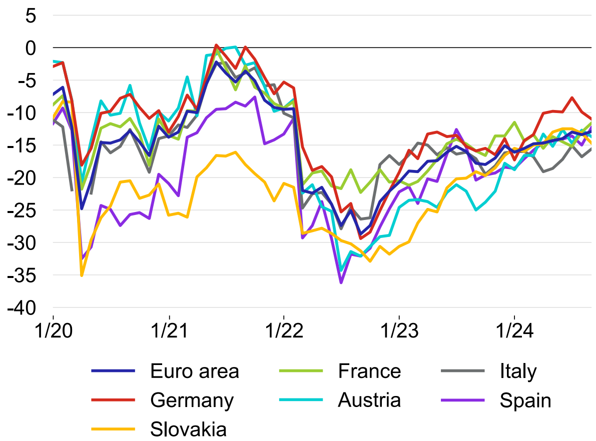
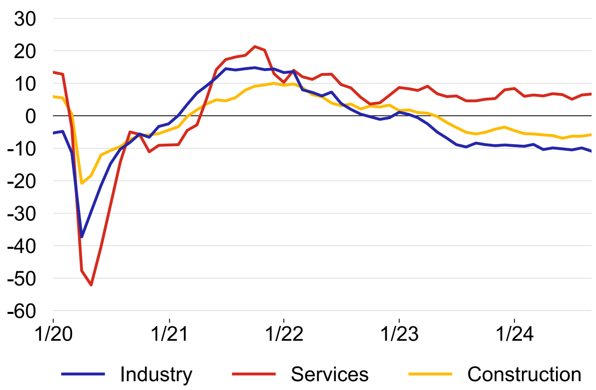


Chart I.3

The situation in services in the euro area is positive, unlike in industry

confidence indicators; seasonally adjusted; source: European Commission



been beset by ailing industry (due to close links to Germany and to the energy crisis) and considerable consumer restraint, as the saving rate remains high despite buoyant wage growth. Like Germany, the Austrian economy has suffered a loss of competitiveness in recent years.

This contrasts with Spain, which is currently doing well economically and is therefore the driver of effective euro area growth. It is benefiting from tourism and solid domestic demand thanks to rising consumer confidence. France enjoyed a short-term lift from the Olympic Games. According to the PMI indicator, however, services fell again in September, even though consumer confidence increased. Slovakia remains a swiftly growing economy and should stay so next year. According to an NBS estimate, the announced fiscal consolidation package will not significantly slow the economy until 2026. However, the future course of fiscal policy represents a risk for many other euro area countries due to necessary consolidation.

According to the forecast, GDP in the effective euro area will grow by 0.5% on average in 2024 as a whole[3] and accelerate to around 1% next year. This will foster a gradual narrowing of the negative output gap, which, however, will not close completely until after the end of the forecast horizon.

This year's decline in industrial producer prices will fade out next year, mainly due to the energy component

The Brent crude oil price mostly declined in Q3 due to an expected weakening of Chinese demand and highly negative investor sentiment. In early October, it returned to USD 75 a barrel as the geopolitical situation in the Middle East escalated. However, it remains highly volatile, due partly to institutional investors building up huge speculative positions and quickly closing them again when events take an unexpected turn. The market outlook for the Brent price remains slightly falling (see Chart I.4) towards USD 73 a barrel at the end of 2026. Refinery fuel margins are under pressure from a structural weakening of demand (mainly in China). Following a temporary decline in mid-September, the price of natural gas in Europe returned to EUR 40/MWh. This was again due to the escalation of the Middle East conflict, as stocks in Europe are at a seasonal high, supplies are stable and demand from industry remains weak. However, the market expects prices of gas – and hence also electricity – to rise slightly during the winter. The industrial metals price index surged in September

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3 According to Eurostat's flash estimate, GDP in the effective euro area rose by 0.3% quarter on quarter and by 0.6% year on year in 2024 Q3. This figure was published on 30 October 2024, i.e. after the closing date of the forecast.

Chart I.4

The Brent crude oil price fell in Q3 but rose again in October; however, its outlook remains slightly falling

prices of selected commodities; index: February 2022 = 100; European gasoline price (ICE) on ARA exchanges; source: Bloomberg, CNB calculation

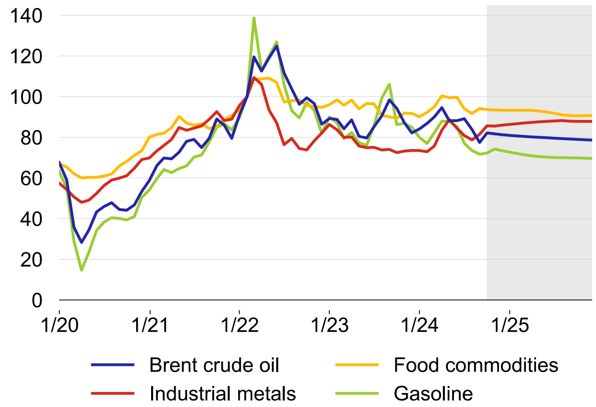


Chart I.5

The year-on-year decline in industrial producer prices in the effective euro area this year is due predominantly to energy prices, whose negative contribution will fade out in 2025

y-o-y changes in %; contributions in pp; seasonally adjusted

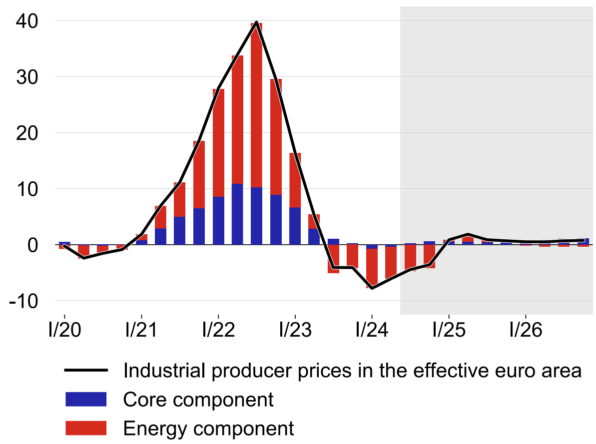
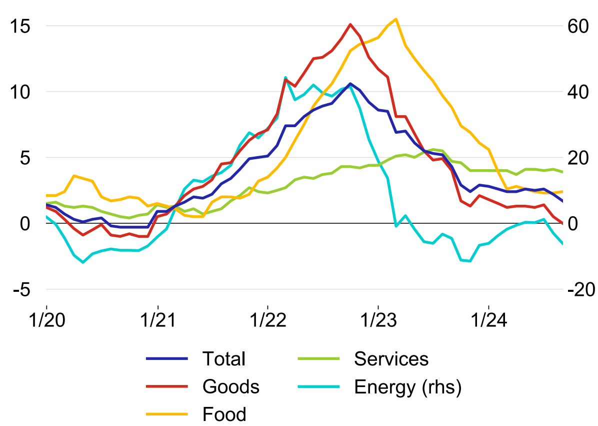


Chart I.6

Unlike goods inflation, services inflation in the euro area remains elevated

components of euro area HICP inflation; y-o-y changes in %



and October, with prices supported by the interest rate cut in the USA and the growth stimulus measures announced by the Chinese government. However, they are not expected to rise much further. The food commodity price index was virtually flat in Q3 and its outlook is slightly falling.[4]

The decline in industrial producer prices in the effective euro area this year is being driven by the energy component (see Chart I.5), i.e. by a year-on-year fall in prices of energy (above all natural gas and Brent crude oil). The negative contribution of energy prices will fade out next year. Following a decline in the first half of the year, core prices have been rising only slightly since Q3. They will not increase strongly in the period ahead either, mainly due to a worse economic activity outlook for the effective euro area. Overall, industrial producer prices will fall by 5.5% this year and rise only slightly in the subsequent two years (by 1.1% in 2025 and 0.6% in 2026). Slovakia will record the largest price decline this year, whereas Germany will see the smallest fall. Next year, industrial producer prices are expected to grow in most euro area countries.

The decline in the extreme cost pressures of previous years and the tight monetary conditions are gradually passing through to falling consumer price inflation in the euro area. The contribution of industrial goods prices to headline inflation has fallen substantially this year. Growth in food prices remains moderate. However, growth in services prices is still strong (see Chart I.6) as a result of robust demand in this segment. Wages, which are the main cost factor in services, are also playing a role. Wage growth remains elevated due to the strong labour market. According to data on negotiated wages, however, the growth is weakening gradually. This could help reduce inflation pressures in the services sector going forward. Inflation in the effective euro area will slow to 2.5% for this year as a whole and will be just above the 2% target on average in the subsequent two years. Slovakia will record the highest inflation this year, while Italy will record the lowest.

The ECB lowered interest rates in October, and the market is raising its bets on another cut in December; the CNB's forecast involves an expert adjustment that reduces the decline in the 3M EURIBOR expected by the market

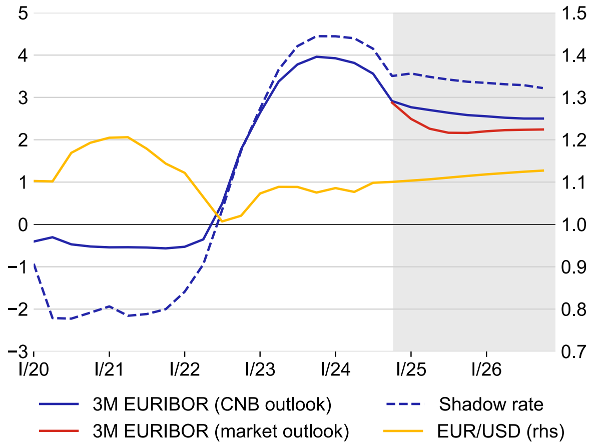
The ECB cut interest rates by 0.25 pp at its October meeting, as expected by the market and analysts. The press conference was dovish. President Lagarde said that the disinflationary process was faster than expected and that the ECB expected inflation to reach 2% in the course of 2025, not at the end. The September inflation figure had been lower than

*The **market outlook for the 3M EURIBOR** has been particularly volatile over the last year. It has been a frequent source of significant reassessments of the domestic monetary policy outlooks. It is sensitive above all to the weak economic growth in the euro area (and Germany in particular) and reflects concerns of a recession. On the other hand, the ECB's cautious communication ("policy rates sufficiently restrictive for as long as necessary") has not changed much. The market is also reacting sensitively to new data because the ECB continues to emphasise a data-dependent approach. The ECB has stated that the equilibrium interest rate is higher than before but has not disclosed an estimate; analysts also disagree about its level. Therefore, the path of the market outlook in the CNB's autumn forecast has undergone expert adjustment. It assumes that the ECB will lower its rates more gradually than currently expected by the financial market, which has recently tended to be overly pessimistic.*

Chart I.7

Euro area interest rates will go down further; the decline in the shadow rate will be dampened by an expected decrease in the rate of reinvestment by the ECB

3M EURIBOR and shadow rate in %; nominal USD/EUR rate



4 Although global prices of cocoa and coffee remain very high by historical standards, they are expected to fall substantially over the outlook horizon.

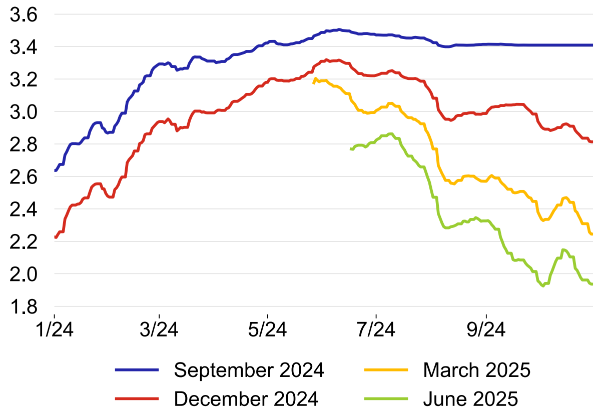
expected. She mentioned concerns about weak economic growth but emphasised that the risk of a recession was low and the ECB still expected a soft landing. The CNB's forecast also works with this scenario (see Chart I.7). In contrast to the ECB's cautious approach, the financial market started to gradually raise its bets on a rate cut of up to 0.50 pp at the December meeting. The market expects the ECB's deposit rate – now officially the main policy rate[5] – to decline to 2% in mid-2025 (see Chart I.8). The latest survey among analysts points to 2.25%. The risk of a faster decline in ECB rates in line with market expectations, coupled with a worse economic situation, is described in the scenario of an economic downturn in Europe in section IV.

The euro stayed at stronger levels against the dollar in Q3 and is expected to appreciate gradually until the end of the forecast horizon, reaching USD 1.15. Gradual normalisation of monetary policy in the USA is expected as the US labour market steadily cools. However, the subdued euro area economy and, conversely, the solid shape of the US economy are preventing the euro from strengthening faster.

Chart I.8

The market was expecting a rapid decrease in ECB rates at the start of this year, but this did not materialise; current expectations again point to a fairly sharp decline

implied rate for given ECB meeting in % based on overnight indexed swap; ten-day average; source: Bloomberg



COMPARISON WITH THE PREVIOUS FORECAST: Economic developments abroad

		2024	2025	2026	
GDP (in the effective EA)	y-o-y changes in % pp	**0.5** (-0.2)	**0.9** (-0.5)	**1.5** (-0.1)	The growth outlook for the effective euro area has decreased, as the German economy still has not resolved its problems.
Consumer prices (in the effective EA)	y-o-y changes in % pp	**2.5** (-0.1)	**2.1** (-0.1)	**2.1** (0.0)	The slight decline in the consumer price forecast reflects above all a deeper drop in the energy component this year and a lower wage growth outlook next year.
Producer prices (in the effective EA)	y-o-y changes in % pp	**-5.5** (0.4)	**1.1** (0.3)	**0.6** (-0.6)	The forecast for industrial producer prices has shifted up for 2024–2025 due to observed data; its drop in 2026 reflects the worse economic outlook for the effective euro area.
Brent crude oil price	USD/barrel	**80.6** (-3.3)	**75.0** (-5.1)	**73.2** (-3.0)	The Brent price outlook has moved down due to negative market sentiment and lower global demand (in China, among other countries); the oil price outlook remains falling.
3M EURIBOR	% pp	**3.6** (-0.1)	**2.7** (-0.4)	**2.5** (-0.3)	The interest rate outlook has shifted down owing to faster disinflation and slower economic growth in the euro area than in the summer forecast.
Exchange rate	USD/EUR	**1.09** (0.01)	**1.11** (0.02)	**1.12** (0.00)	The expected slight appreciation of the euro against the dollar is little changed compared with the previous forecast; the euro will appreciate from a stronger initial level.

Note: Changes compared to the previous forecast in brackets (a green label indicates an increase in value or a shift to a weaker dollar, while a red label indicates a decrease in value or a shift to a stronger dollar)

5 For details see Changes to the operational framework for implementing monetary policy, 13 March 2024.

II. THE REAL ECONOMY AND THE LABOUR MARKET

After stagnating last year, the Czech economy is this year returning to growth, driven mainly by household and general government consumption. The recovery in household consumption is being supported by renewed growth in real household income due to falling inflation, and by a decline in interest rates. The contribution of net exports to GDP growth is also positive. However, it will soon turn negative owing to subdued external demand and recovering domestic demand. Fixed investment is growing modestly. It will rise only slowly in the private sector due to slow absorption of EU funds and weak external demand and will even decrease slightly in the general government sector. Firms are this year releasing the inventories they amassed over the previous three years. In whole-year terms, GDP will grow by 1% this year and the economy will still operate below its potential. The growth will accelerate to 2.4% next year. This will be aided above all by households' strengthening consumer appetite, supported by still solid real wage growth and rising investment growth. By contrast, the economic expansion will be temporarily hindered by net exports, despite renewed growth in external demand. The labour market tightness will gradually ease further. The previously elevated nominal wage growth will slow gradually.

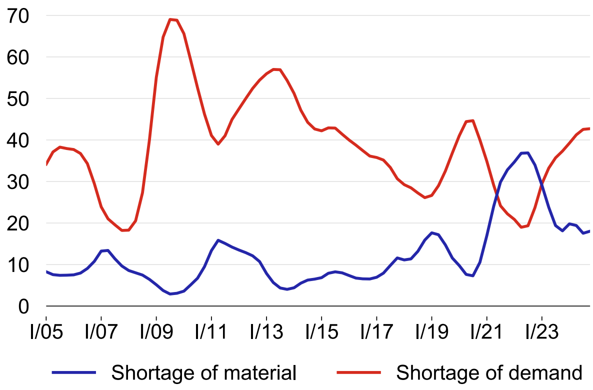
Economic growth will resume this year and pick up markedly next year

This year's recovery in GDP growth is being driven by renewed growth in household consumption, supported above all by rapidly rising real income coupled with falling interest rates. By contrast, still somewhat fragile consumer sentiment will continue to dampen consumption growth in the second half of this year. Export-oriented industrial firms increasingly perceive insufficient demand, especially from abroad, as the main factor limiting production (see Chart II.1). The previously significant contribution of net exports to GDP growth will thus decline but remain positive, contributing to GDP growth to similar extent as household consumption. The contribution of general government consumption, which includes expected expenditure on reconstruction after the September floods, to GDP growth will also be similar. This expenditure will also be reflected in general government fixed investment, which, however, will decline slightly in year-on-year terms due to base effects. Private fixed investment will increase this year, but the growth will be very weak owing to subdued external demand. The problems in global value chains have largely disappeared, as indicated by an absolute decline in inventories in the domestic economy since the end of last year. Inventories will also decline over the next few quarters and their contribution will stabilise at pre-crisis levels in the course of 2025. As a result, domestic economic activity will increase year on year (see Chart II.2).[6] In whole-year terms, GDP will

Chart II.1

The share of firms reporting insufficient demand continues to rise

share of domestic industrial firms in % reporting shortages of materials or equipment and insufficient demand as factor limiting production; series smoothed by HP filter (lambda = 1); source: CZSO business survey



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6 According to the CZSO's flash estimate, Czech GDP increased by 0.3% quarter on quarter and by 1.3% year on year in 2024 Q3. This is in line with the CNB forecast. This figure was published on 30 October 2024, i.e. after the closing date of the forecast.

grow by 1% this year. The growth will pick up to 2.4% in 2025 and stay at that level in 2026.

Household consumption is growing this year on the back of renewed growth in real wages

Household consumption is gradually recovering from its protracted downturn. In quarter-on-quarter terms, consumer spending has been growing since the end of last year. However, it is still lagging behind the strongly positive growth in real wages. This is due to still somewhat fragile consumer sentiment[7] and to the CNB's tight monetary policy stance. The current retail and services leading indicators suggest that quarter-on-quarter growth in household consumption remained similarly weak in Q3 as in Q2. Precautionary motives and concerns about the future economic situation will dampen growth in consumer spending over the next few quarters. However, falling interest rates and still buoyant – albeit slowing – growth in nominal wages and total income will ultimately outweigh these negative effects and quarter-on-quarter growth in household consumption will thus rise gradually. In whole-year terms, it will grow by 1.6% this year (see Chart II.3).

The growth in real (disposable) household income will continue into next year, and consumer appetite will pick up further after interest rates come down further. Pessimistic sentiment will fade away as the economy recovers. Household consumption will thus go up by 2.2% in 2025 and 2.8% in 2026.

Year-on-year growth in households' nominal gross disposable income will slow this year compared to the elevated rates seen in previous years and will fluctuate around 3% until the end of the forecast horizon. It will be driven above all by a broadly stable contribution of wages and salaries (see Chart II.4). The lower growth in gross nominal disposable income this year will be due mainly to a decrease in the contribution from income of entrepreneurs, whose profit margins have been falling. Property income has been declining year on year this year owing to falling interest rates. The negative contribution of taxes is being amplified by the consolidation package, which is also affecting the gradually declining positive contributions of social benefits.

The saving rate will decrease gradually over the next few years

The saving rate has been elevated for several years now (see Chart II.5). This is due to still volatile consumer sentiment (fragile confidence), reflecting households' concerns about the future economic and financial situation. The precautionary motive will thus

Chart II.2

Growth in domestic economic activity will accelerate

y-o-y changes in %; prices of 2020 (chain-linked); seasonally adjusted; confidence interval

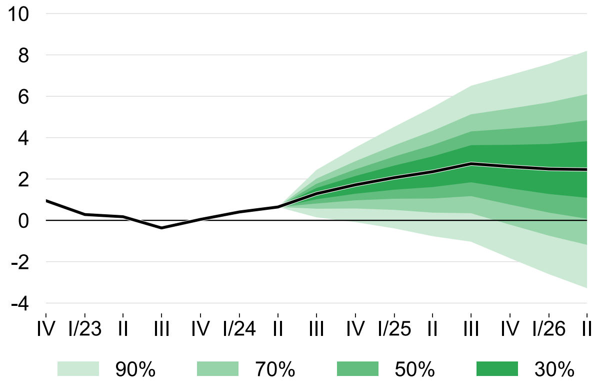


Chart II.3

Growth in household consumption will gain momentum gradually; general government consumption will slow for the rest of the year and continue to grow at a subdued pace

household and general government consumption; y-o-y changes in %; prices of 2020 (chain-linked); seasonally adjusted

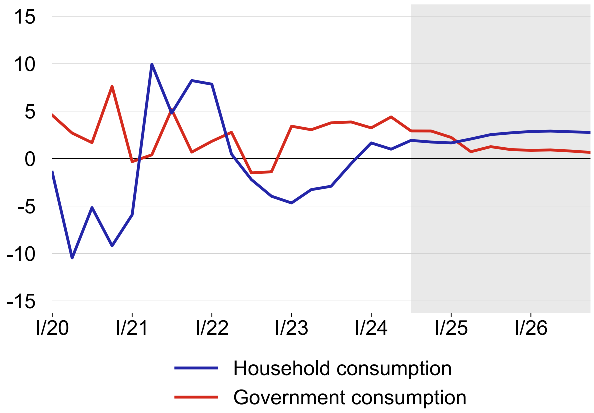
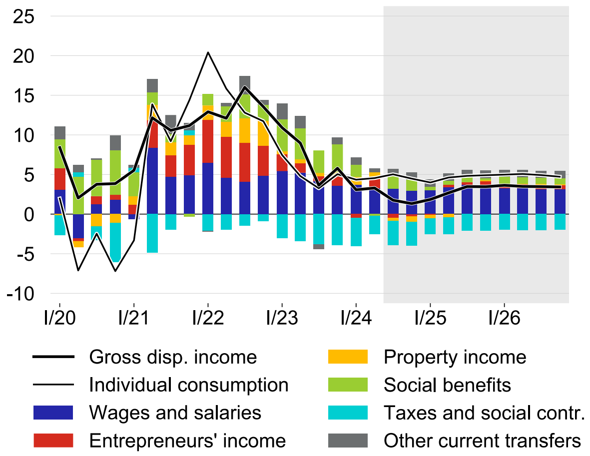


Chart II.4

Growth in nominal disposable income is slowing this year but will pick up pace again over the next few years

household consumption and gross disposable income; y-o-y changes in %; contributions in pp; current prices; seasonally unadjusted



7 According to the October business cycle survey data, overall confidence in the economy was flat at a similar level as in September amid a slight deterioration in business confidence and an improvement in consumer sentiment.

continue to affect savings over the next few quarters, as will still positive real interest rates. However, falling interest rates and fading negative sentiment will gradually prevail over the next two years. This, together with slowing but still above-average wage growth, will cause the saving rate to decline gradually towards its usual level.

Export growth will accelerate over the next two years as external demand recovers; imports will also increase significantly

Export activity was subdued in the first half of this year and will remain so for the rest of the year. This will be due to lacklustre performance of other economies, especially the current economic stagnation of Germany, the Czech Republic's largest trading partner. However, quarter-on-quarter export growth was aided by exports of forced stocks of unfinished products, which have been accompanied by a fall in inventories in absolute terms since the end of last year. This factor will affect exports until the start of next year and, together with a gradual recovery in external demand, will cause growth in Czech exports to accelerate (see Chart II.6).

Imports rose somewhat more than exports in quarter-on-quarter terms in the first half of this year due to recovering domestic demand. Import growth was solid despite a reduction of built-up stocks, which did not have to be imported. It will accelerate in the rest of this year on the back of gradually increasing domestic demand and a recovery in import-intensive exports. In 2025, import growth will strengthen further due to swift growth in household consumption and fixed investment. In 2026, it will slow (see Chart II.6). Net exports continue to contribute significantly to GDP growth this year. Next year, however, they will dampen domestic economic growth slightly despite a recovery in external demand. In 2026, their effect will be broadly neutral.

Fixed investment will be subdued this year and recover significantly next year

Gross fixed capital formation rose only very modestly overall in the first half of the year, driven by the private sector. By contrast, general government investment fell slightly. The forecast expects similar developments in the second half of this year. General government investment will decline by around 1% in 2024 as a whole, due mainly to base effects[8] and also to the government's consolidation efforts. The initially unplanned investment activity at the year-end resulting from the need to repair flood damage will change nothing about this. By contrast, private investment will continue to rise. Its growth will pick up as external demand recovers and domestic and foreign interest

8 General government expenditure increased last year due to a one-off purchase of military helicopters for CZK 14 billion.

Chart II.5

The saving rate will decline from its current elevated level to close to its usual long-term level due to improving sentiment and falling interest rates

households' saving rate in %; seasonally adjusted

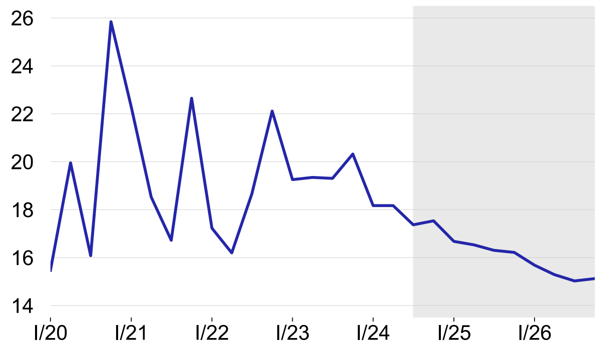
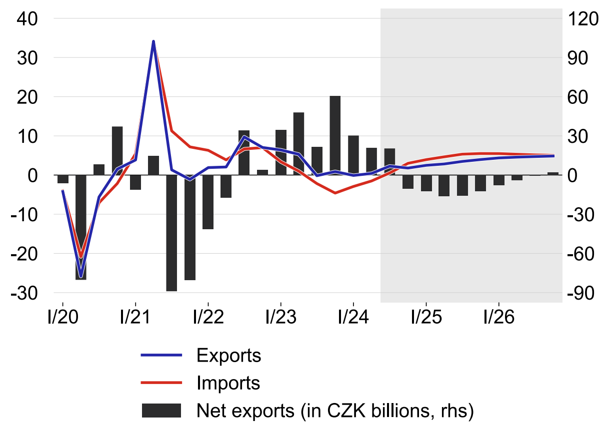


Chart II.6

Export and import growth will gradually accelerate this year and the next as external and domestic demand gradually recovers

real exports and imports of goods and services; y-o-y changes in % for exports and imports and in CZK billions for net exports; seasonally adjusted



rates fall. However, it will be dampened by a slow start to the absorption of EU funds in the new programme period. Fixed investment will grow by around 1% overall in 2024 (see Chart II.7).

General government investment will start to grow again in 2025, aided by expected faster absorption of European funds and money from the National Recovery and Resilience Plan. Private investment growth will also accelerate, due, among other things, to an investment by chip manufacturer onsemi in the car industry and automotive technology. Overall, fixed investment will grow at a pace of around 3% next year.

Firms will release a large part of their inventories accumulated in the previous three years. The forecast expects stocks to decline until the start of next year, though at a slowing pace. Firms are gradually going back to just-in-time planning, which implies a return to low additions to inventories (see Chart II.8). As a result, change in inventories is making a negative contribution to year-on-year growth in gross capital formation this year. Next year, by contrast, its contribution will be strongly positive. Gross capital formation growth will thus be very volatile, falling by more than 4.5% this year but rising by 7.5% next year (see Chart II.7).

Fiscal policy is significantly dampening GDP growth this year and will have a neutral effect next year

Real government consumption growth remains elevated this year (see Chart II.3). Cuts in operating expenditure under the government's consolidation package will be offset by extraordinary expenditure on reconstruction following the floods. Next year, real government consumption growth will decrease due to additional savings stemming from this year's fiscal package. The forecast for nominal general government consumption in 2025 also takes into account the announced brisk growth in public sector pay. Growth in nominal government consumption will slow gradually, due mainly to cuts in operating expenditure and the declining effect of extraordinary expenditure after the floods.

Fiscal policy is significantly dampening GDP growth this year (see Chart II.9), owing to the consolidation package,[9] the definitive termination of energy support

Chart II.7

Growth in total gross capital formation will be volatile due to inventories, while growth in private fixed investment will accelerate gradually

investment activity; y-o-y changes in %; contributions in pp; prices of 2020 (chain-linked); seasonally adjusted

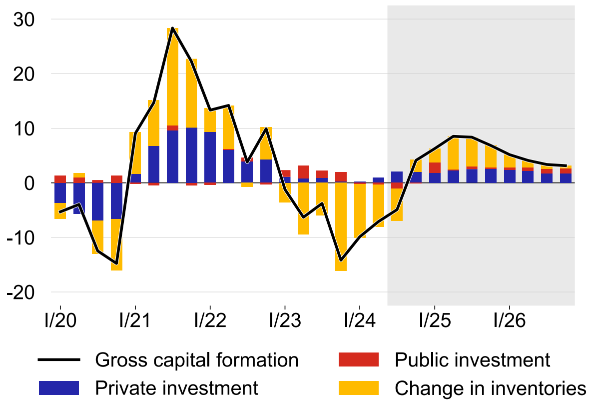
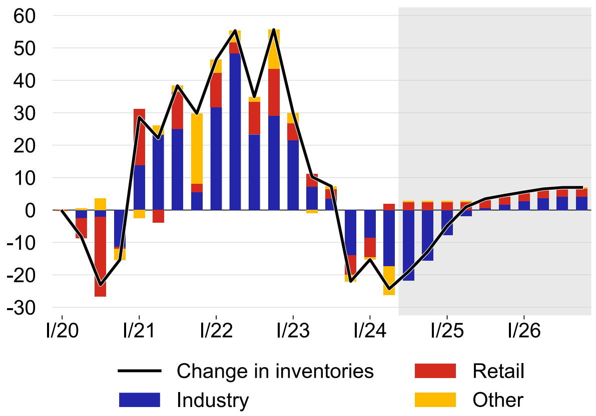


Chart II.8

Change in inventories is negative in the course of this year; inventories will return to low positive growth next year

change in inventories in CZK billions; prices of 2020 (chain-linked); seasonally adjusted



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9 The overall fiscal effect of the consolidation package is equal to −1.0% of GDP in 2024. Including further measures not included in the package, the fiscal impulse is approximately −0.7 pp to GDP growth this year (the previous forecasts excluding the effect of unexpected flood expenditure estimated this effect at approximately −1 pp). In 2025, the fiscal effect of the package will be an additional −0.3% of GDP (although increased government investment will have the opposite effect on the fiscal impulse). On the revenue side, the consolidation package includes the following measures: an increase in excise duties, changes to VAT rates, an increase in real property tax, an increase in contributions

measures and a decrease in pension expenditure stemming from the fading effect of the reduction of the extraordinary increase in pensions last year. Extraordinary expenditure related to reconstruction after the floods is having the opposite effect. In 2025, the overall effect of fiscal policy will be broadly neutral, as the additional (residual) slightly dampening effect of the consolidation package will be offset by expected faster absorption of EU funds. The forecast assumes that fiscal policy will have a slightly expansionary effect in 2026.[10]

The negative output gap of the Czech economy will gradually close

The output gap has been negative in recent years due to the economic downturn. It started closing at the end of last year. However, faster closure is being hindered by a surprisingly muted recovery in domestic household consumption growth and by the persisting problems of Germany, our largest trading partner. However, based on an analysis of the domestic and foreign economy, the forecast expects these negative factors to dissipate gradually. At the same time, there will be a major reversal in the gross capital formation trend towards growth, with inventories and fixed investment both contributing. The negative output gap is thus expected to continue closing as growth in domestic and external demand recovers gradually. The fiscal consolidation package and the previous tight monetary policy are slowing the pace of closure of the output gap this year, broadly in line with the previous forecasts. The output gap will almost close next year as these effects drop out, and the economy will be very close to its potential in 2026 as well (see Chart II.10). Growth in potential output itself will pick up slightly towards its medium-term rate (2.5%) due to gradually recovering trend growth in labour productivity.

Chart II.9

Fiscal policy will significantly dampen GDP growth this year, due mainly to the consolidation package

fiscal impulse; contributions to GDP growth in pp

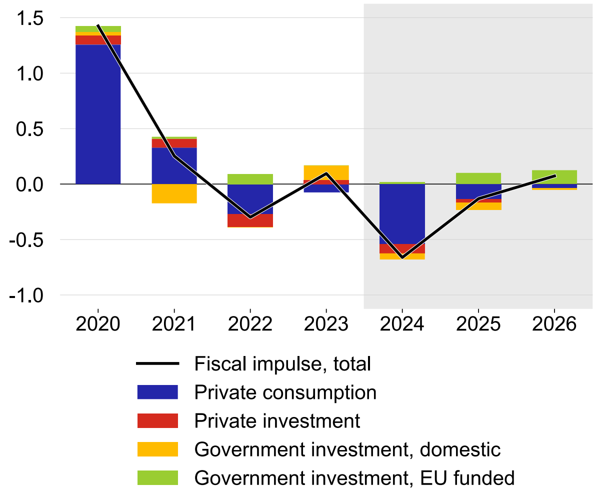
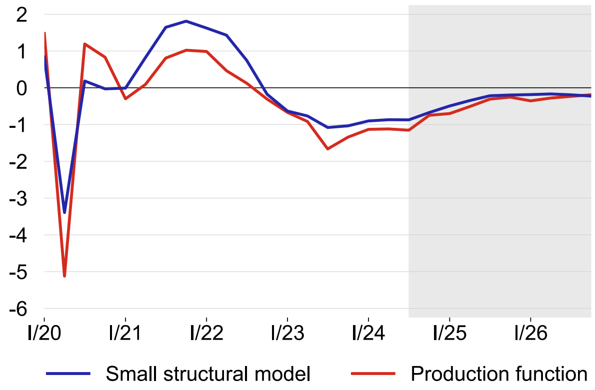


Chart II.10

The economy will be only slightly below its potential from 2025 onwards

output gap in % of potential output



for the self-employed, adjustments to personal and corporate income tax, the abolition of tax exemptions, the introduction of sickness insurance for employees, and contributions arising from agreements to complete a job. On the expenditure side, it includes cuts in subsidies for entrepreneurs, a temporary reduction in the volume of public sector pay and cuts in operating and other expenditure.

10 The CNB's fiscal forecast takes into account all the discretionary measures on both the revenue and expenditure sides contained in the draft state budget for 2025, including budgetary documentation.

COMPARISON WITH THE PREVIOUS FORECAST: The real economy and the labour market

		2024	2025	2026	
GDP	y-o-y changes in % pp	**1.0** (-0.2)	**2.4** (-0.3)	**2.4** (0.1)	The GDP outlook for this year and the next is lower than in the previous forecast due to weaker external demand and a more gradual recovery in household consumption.
Household consumption	y-o-y changes in % pp	**1.6** (-0.4)	**2.2** (-1.3)	**2.8** (-0.3)	The household consumption forecast is lower due to lower growth in real wages and worse consumer sentiment.
Government consumption	y-o-y changes in % pp	**3.4** (0.8)	**1.3** (0.6)	**0.8** (0.1)	Government consumption is slightly higher due to higher observed non-wage expenditure and also to expenditure on flood repairs in late 2024 and early 2025.
Gross fixed capital formation	y-o-y changes in % pp	**0.9** (1.6)	**2.9** (-0.8)	**2.7** (-0.3)	Growth in fixed investment will be higher this year due to stronger observations in Q2 and expenditure on flood repairs; weaker external demand will predominate in the next two years.
Net exports	contr. to GDP growth pp	**0.9** (-0.1)	**-0.8** (0.1)	**-0.1** (0.0)	The changes in the contributions of net exports to GDP growth compared to the summer forecast are negligible.
Number of full-time equivalent employees	y-o-y changes in % pp	**0.2** (-0.2)	**0.2** (-0.1)	**0.2** (-0.1)	The slower growth in the number of full-time equivalent employees this year mainly reflects lower data in Q2; growth in 2025 will be affected by a slower expected economic recovery.
Unemployment (ILO)	% pp	**2.7** (-0.1)	**2.9** (0.0)	**3.0** (0.0)	The outlook for the general unemployment rate is almost unchanged from the previous forecast.
Average monthly nominal wage	y-o-y changes in % pp	**6.4** (-1.0)	**5.7** (-0.7)	**5.1** (-0.1)	The slower wage growth in a situation of a lowered outlook for domestic economic activity is due also to lower observations in the first half of this year.

Note: Changes compared to the previous forecast in brackets (a green label indicates an increase in value and a red label a decrease)

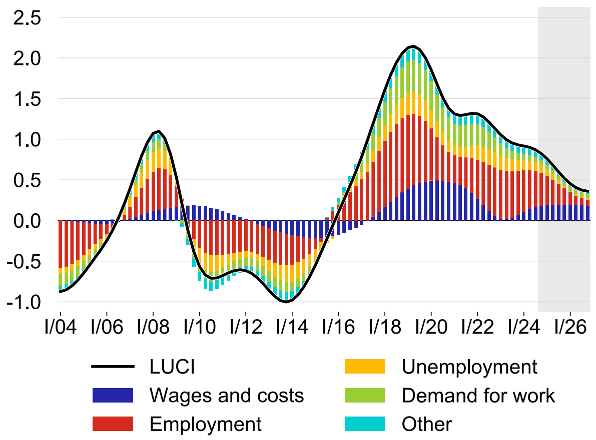
The labour market will continue to cool gradually

From the perspective of the LUCI, the gradual cooling of the Czech labour market – linked with the domestic economic downturn last year – is continuing (see Chart II.11). Employment continues to contribute to persisting (albeit now only moderate) labour market tightness, as firms are retaining staff despite the subdued economic activity[11] and labour productivity is thus not rising. The contribution of employment will decrease in the future, mainly because of a gradual draining of the labour pool and a fall in demand for labour. Firms are now more cautious about recruiting. This is related to the still uncertain situation in industry linked to weaker demand from Germany. The continuing steady increase in unemployment indicators is leading to a gradual reduction in the contribution of unemployment in the LUCI. This reflects the usual delay in the response of the labour market to the previous economic contraction. By contrast,

Chart II.11

From the perspective of the LUCI, the tightness in the labour market will decrease further

LUCI; vertical axis shows standard deviations



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11 The thirteen-month moving average of the Labour Hoarding Indicator compiled by the European Commission points to an increased share of firms that will not lay off employees even if they expect their output to worsen.

wages and costs will make a positive contribution to labour market tightness over the forecast horizon.

Year-on-year real wage growth will remain elevated from the long-term perspective

The real wage abruptly returned to year-on-year growth in early 2024 after more than two years of decline. This was due to high, albeit slowing, wage growth in nominal terms and a decline in inflation to close to the CNB's 2% target. This situation will continue until the end of the forecast horizon.

Year-on-year average nominal wage growth in market sectors will remain high from a historical perspective[12] for the rest of this year (see Chart II.12) and will thus continue to reflect earlier inflation pressures. Wage growth will be solid in year-on-year terms until mid-2025, due to strong wage growth in 2024 Q1 and to a gradual economic recovery over the outlook horizon. It will then gradually return to its long-term average. This trend appears to have started in Q2, when quarter-on-quarter wage growth slowed and the contributions of wages in manufacturing and wholesale and retail fell sharply.[13] The minimum wage is to be increased by CZK 1,900 (10%) to CZK 20,800 in January 2025. The forecast assumes a gradual increase in the minimum wage in subsequent years to 47% of the average wage in 2029. The forecast includes a significant rise in public sector pay in non-market sectors in January 2025 (after a period of moderate growth), as well as legislative changes to the cascade of guaranteed salaries.[14] Wages and salaries will grow faster in non-market sectors (6.1%) than in the market sector (5.7%).

Growth in the nominal wage bill this year and in the years ahead is affected mainly by growth in the average wage. In real terms, the wage bill returned to year-on-year growth at the start of this year, due to a fall in inflation, and kept rising in Q2 (see Chart II.13). Growth in the real wage bill will remain positive at around 3%, with minor fluctuations, until the end of the forecast horizon.

The number of full-time equivalent employees will be flat for the rest of this year; unemployment will grow very slightly

Chart II.12

Despite slowing, nominal wage growth will remain high from the long-term perspective

nominal wages; y-o-y changes in %; seasonally adjusted

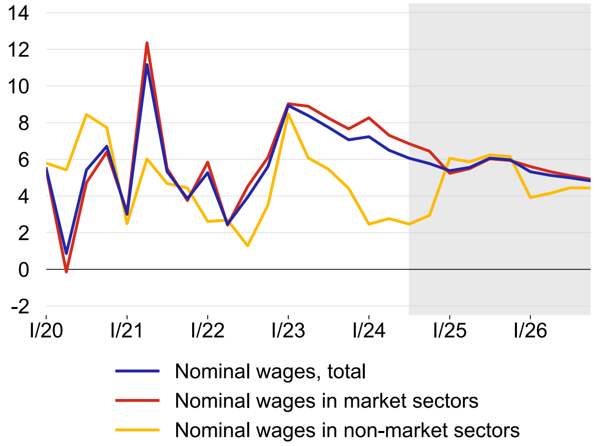
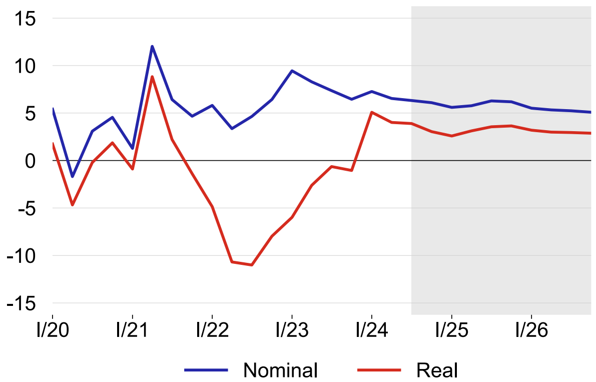


Chart II.13

Growth in the real wage bill will remain elevated and will thus help the growth rate of household consumption return to the long-term average

wage bill; y-o-y changes in %



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12 The forecast assumes long-term equilibrium wage growth of 4.5% in the market sector.

13 There is increased uncertainty about wage growth in Q3 linked with high volatility of the monthly wage indicators during the summer months. The volatility was caused by legislative changes and a large difference in the number of working days compared with last year.

14 The cascade of guaranteed wages will be abolished in the wage sector at the start of next year, and unlike in the salary sector, only the minimum wage will remain mandatory for the wage sector. In the salary sector, the cascade of guaranteed wages will be replaced by a cascade of guaranteed salaries, and the number of guaranteed salary classes (formerly wage classes) will be reduced from eight to four.

Employment expressed in terms of the number of full-time equivalent employees[15] will remain flat in quarter-on-quarter terms and will increase slightly year on year (see Chart II.14). This is due, among other factors, to gradual exhaustion of the labour supply and employer caution in recruitment owing to the previous economic downturn. Leading indicators are still sending mixed signals. The European Commission survey expects the number of employees to decline over the next three months. By contrast, the index of expected employment and other high-frequency and leading indicators[16] suggest continued corporate recruitment.

Following a slight increase in 2023, the general unemployment rate will be broadly flat this year, reflecting companies' efforts to retain their work teams in an environment of subdued demand. The number of people out of work will return to slow growth in the following years due to the lagged impact of the previous economic downturn (see Chart II.14). However, it will stay very low by both historical and international standards. The forecast expects a similar trend in the share of unemployed persons.

Domestic cost pressures will ease in 2025 due to slowing wage growth and a gradual resurgence of growth in labour efficiency

Growth in domestic costs eased further in 2024 Q3 but remained elevated (see Chart II.15). This was due predominantly to continued buoyant wage growth in market sectors, whose quarter-on-quarter growth slowed after a one-off acceleration at the start of this year. The repercussions of the previous high inflation will be reflected in a noticeable contribution of wages over the outlook horizon. The positive contributions of the price of capital to growth in domestic costs will reflect increasing domestic economic output. However, the increase in economic activity will be driven mainly by additions to inventories in late 2024 and early 2025. This, along with modest quarter-on-quarter growth in employment, will improve labour efficiency only gradually. Labour efficiency will thus initially dampen growth in costs only slightly. It will also improve as growth in the other components of GDP gradually picks up. Together with slowing wage growth, this will lead to a gradual decline in domestic cost pressures to close to levels consistent with price stability in 2026.

Chart II.14

The number of full-time equivalent employees will rise slightly; unemployment will increase only slowly

employment (full-time equivalent); y-o-y changes in %; general unemployment rate in %; seasonally adjusted

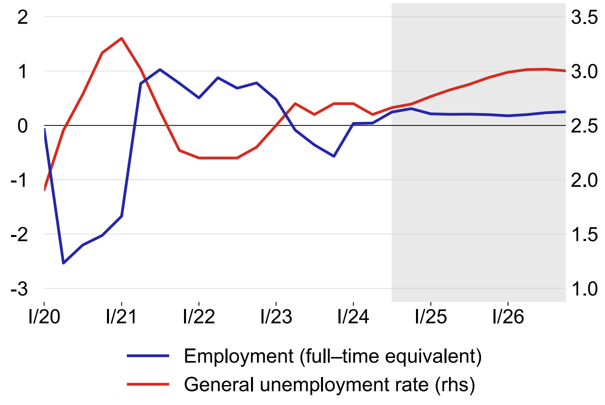
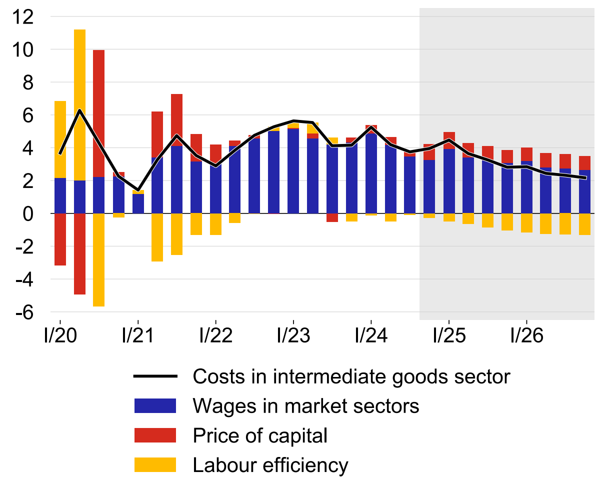


Chart II.15

A continued slowdown in quarter-on-quarter wage growth, along with gradual renewed growth in labour efficiency, will be reflected in a decline in domestic cost pressures from the start of next year

costs in intermediate goods sector; q-o-q changes in %; contributions in pp; current prices; annualised



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15 For better interpretability of labour market developments, employment is now described using the series of the number of full-time equivalent employees (instead of total employment from the LFS).

16 For 2024 Q4, the Manpower Group index of expected employment is signalling a continuation of the rise in the number of employees observed in previous quarters. The Google Trends scores for "unemployment" and "unemployment benefit" have remained low in recent weeks. In 2024 Q3, the total number of vacancies increased very slightly compared to the previous quarter.

III. INFLATION

Inflation was close to the CNB's 2% target during the summer holidays. In September, it accelerated further into the upper half of the tolerance band, due mainly to rising growth in food prices. Headline inflation will temporarily increase further in Q4 on the back of a continued rise in annual food price inflation. It will thus briefly rise slightly above the upper boundary of the tolerance band around the inflation target at the turn of the year. The renewed decrease in inflation early next year will be due mainly to a sharp drop in administered price inflation in January. Core inflation will remain broadly stable in the same period, despite depreciation of the koruna. The stability of inflation in this key segment reflects the current anti-inflationary demand environment in the domestic economy and abroad, which will persist into the future. The aforementioned slight weakening of the koruna will be offset by slowing growth in domestic labour costs and a continued gradual correction of the until recently highly elevated profit margins of domestic producers, retailers and service providers. Headline and monetary policy-relevant inflation will thus decline gradually next year and will be close to the CNB's 2% target over the monetary policy horizon amid a continued decline in interest rates over the next few quarters.

Inflation will be close to the upper boundary of the tolerance band around the inflation target at the turn of the year

Inflation was close to the 2% target in the summer. The upswing in inflation in September was due mainly to higher growth in food prices (followed by rising prices in education). Inflation will pick up further in Q4 and will be at the upper boundary of the tolerance band around the inflation target on average (see Chart III.1) and briefly increase above the inflation target at the turn of the year. This will be due mainly to a continued rise in annual food price inflation. The positive contribution of core inflation and the negative contribution of fuel prices will remain roughly stable. The same will apply for the market components of inflation in 2025 Q1. By contrast, the contribution of administered prices – still elevated throughout 2024 – will decrease significantly in January (see Chart III.2).

Administered price inflation will remain above-average at the end of this year and will fall at the start of 2025

Annual administered price inflation remained close to 6% in Q3 (i.e. still elevated from a historical perspective), even though electricity and gas suppliers further reduced the commodity component of housing-related energy prices in the summer (see Chart III.3). An increase in the administered component of energy prices, a rise in water supply and sewerage collection charges, the reintroduction of the fee for renewable energy sources right at the start of the year, a significant increase in the price of the road toll vignette in March and a sharp rise in the prices of some items in the education category in September have contributed to the still high annual administered price inflation this year. On average, it will stay close to 6%

Chart III.1

Inflation will be close to the upper boundary of the tolerance band around the target at the turn of the year and will then start to decline gradually towards the 2% target

headline inflation; y-o-y in %; confidence interval

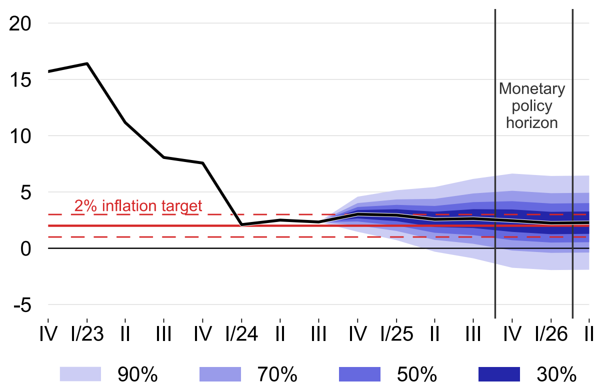
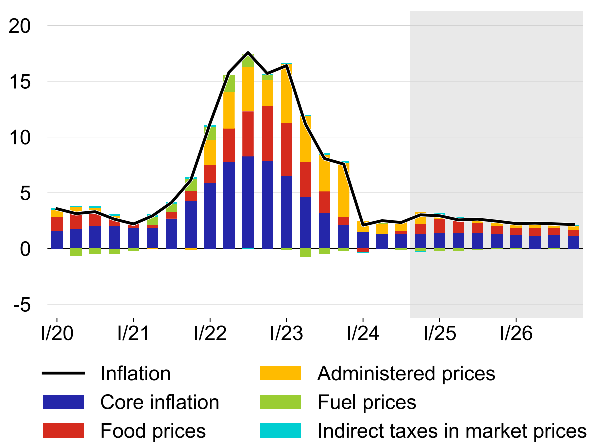


Chart III.2

The contribution of food prices will increase over the next few quarters

structure of inflation; y-o-y changes in %; contributions in pp



this year and will then drop below 2% in 2025, due mainly to a year-on-year decrease in electricity and gas prices, despite the planned increase in licence fees in January,[17] an expected continued increase in the administered component of energy prices and growth in prices of many other items.

Market price inflation will rise above 2% next year

Market price inflation has been subdued so far this year (see Chart III.4). Companies repriced to only a limited extent at the start of 2024 relative to the still high growth in their costs. Retailers' profit margins thus decreased and the negative contribution of change in the surcharge on costs dampened inflation. The contribution of the surcharge on costs remains negative over the outlook, as the positive and decreasing gap in mark-ups will close at the start of 2026 due to the still tight monetary policy. However, the elevated growth in costs will be only partially offset by the decline in margins next year, so market price inflation will rise temporarily above 2%.

The elevated overall cost pressures will decline next year amid a gradual decrease in the inflationary effect of the domestic economy and import prices

Growth in total costs rose in 2024 Q3 (see Chart III.5) due to an increase in foreign prices of energy and some core import prices, which reflected rising prices of some food commodities on international exchanges. The positive contribution of import prices was also fostered by a slight weakening of the koruna in recent months. Costs will continue to rise at an elevated pace in the coming quarters, affected by continued growth in import prices and strong domestic cost pressures. The latter stem mainly from above-average nominal wage growth, which will not be offset by corresponding productivity growth. In quarter-on-quarter terms, however, wage growth will start to slow gradually in the course of next year, causing growth in total costs to decline. This will also be fostered – despite a slightly weakening koruna – by the contribution of energy import prices gradually turning negative. Growth in total costs will thus converge to its long-term steady-state level of 2% at the end of next year and stay close to it in 2026. Growth in costs will also reflect ongoing price convergence, which leads to traditionally higher services inflation than goods inflation within core inflation.

17 The government approved an increase in the television licence fee from CZK 135 to CZK 150 and the radio licence fee from CZK 45 to CZK 55. These fees were last increased in 2008 and 2005 respectively. At the same time, there are plans to expand the range of payers of these fees. However, it is possible (given the busy programme in Parliament) that the relevant bill will not be passed in time to come into force in January 2025.

Chart III.3

Administered price inflation will fall significantly at the start of 2025 and stabilise close to 2% over the next two years

administered prices; y-o-y changes in %; contributions in pp; including taxes

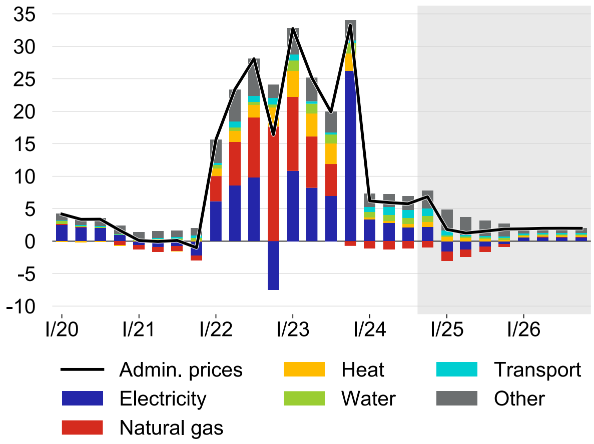
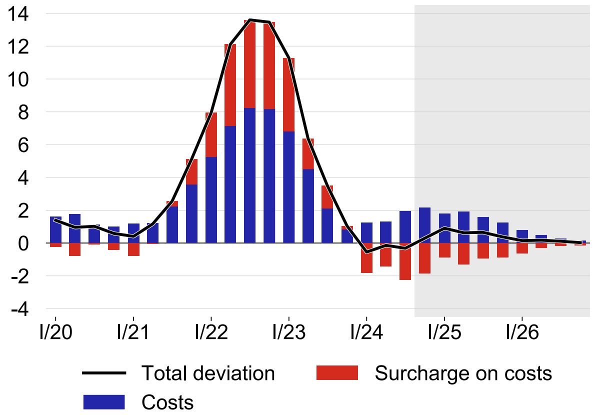


Chart III.4

Persisting elevated growth in costs will foster further price growth, while a decreasing surcharge on costs will dampen it

deviation from steady-state 2% y-o-y growth; contributions in pp

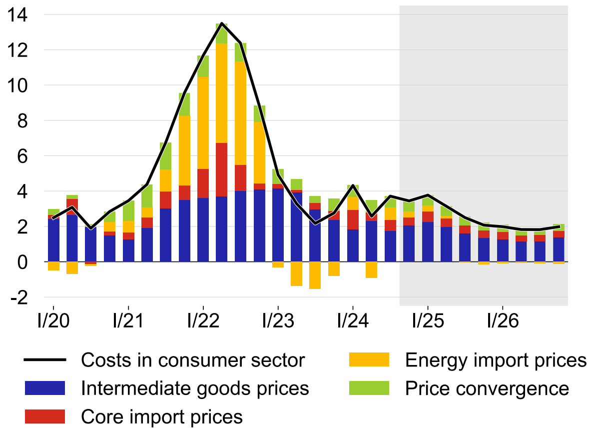


Note: The contribution of the surcharge on costs contains the gap in mark-ups in the sectors of consumer and intermediate goods and services.

Chart III.5

The currently still slightly elevated overall cost pressures will ease next year

costs in consumer sector; q-o-q changes in %; contributions in pp; current prices; annualised



Core inflation will be broadly stable

Core inflation stayed just above 2% in 2024 Q3, thanks in part to tight monetary policy. Growth in non-tradables prices stood close to 4%, while growth in tradables prices was only slightly positive. Core inflation will remain stable in the final months of this year. Still subdued industrial producer price inflation abroad and its spillover to domestic price categories will have an anti-inflationary effect. Conversely, relatively brisk growth in wages in the Czech Republic and a moderate depreciation of the koruna will have an inflationary effect. The contribution of imputed rent will gradually increase (see Chart III.6), while a greater-than-expected pick-up in its growth due to a recovery of the housing market represents one of the risks of the forecast. Despite the increasing contribution of imputed rent, core inflation will, however, remain close to 2% over the entire forecast horizon, due in part to the tight monetary policy to date.

Food price inflation will go up further in the coming quarters

Growth in food, beverage and tobacco prices went up during summer, due to both base effects and a rise in the price level in this category driven in part by a sharp jump in prices of some imported food commodities (for example, coffee and cocoa) and certain foods (milk and butter). These factors will continue to have an effect in Q4 and annual food price inflation will thus go up further (see Chart III.2).

Fuel prices will go down further year on year in the quarters ahead

Annual fuel price inflation turned negative in August. Petrol and diesel prices at filling stations then fell by more than 10% year on year in September. Fuel price inflation will remain negative in the following quarters, mainly because of slightly falling oil prices, whose effect will be dampened by a modest weakening of the koruna.

Headline inflation will be slightly above monetary policy-relevant inflation

At the start of 2024, the changes to indirect taxes in the consolidation package had a mixed effect on consumer prices and were slightly inflationary overall. The inflationary measures included a 10% increase in excise duties on tobacco and alcohol. Conversely, a reduction in the number of VAT rates and the transfer of selected groups of goods and services between these rates had an anti-inflationary effect. Overall, these changes had slightly positive first-round (accounting) effects (see Chart III.7). At the same time, the changes to VAT on some items did not pass fully through to prices. These second-round effects ran in both directions and were negligible overall. Excise duty on tobacco and alcohol will be raised again at the start of next year, when it will go up by 5% and 10%

Chart III.6

Core inflation will stay near 2% amid a gradually increasing contribution of imputed rent

y-o-y changes in %; contributions in pp

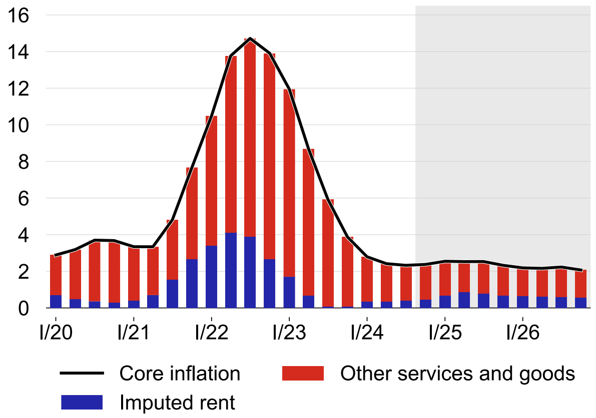
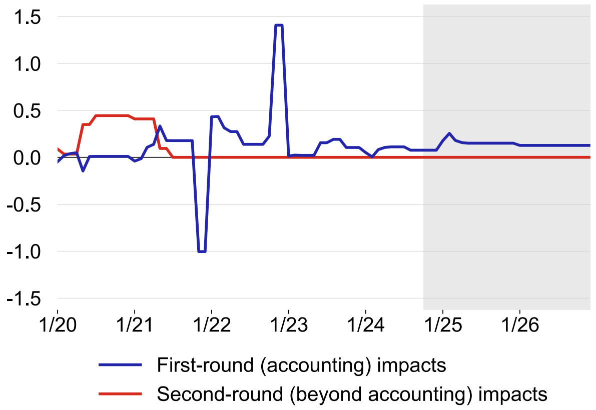


Chart III.7

The effects of changes to indirect taxes this year reflect the numerous changes to VAT and excise duties in the consolidation package and, in the next two years, an increase in excise duties on tobacco and alcohol

first-round and second-round effects of tax changes; contributions to annual inflation in pp



We distinguish two types of direct effects on prices in relation to ***changes to indirect taxes*** *– first-round effects (or accounting effects in the items concerned) and second-round effects (going beyond accounting effects in the items concerned). The first-round effects are the calculated price changes due to the indirect tax changes implied by full (accounting) pass-through of the tax changes to prices of the relevant items of the consumer basket. The second-round effects capture the immediate price changes going beyond the first-round effects and may be positive or negative. The second-round effects affect both monetary policy-relevant inflation and headline inflation. The CNB applies escape clauses to the first-round effects of indirect tax changes and in its forecast sets interest rates with regard to the outlook for monetary policy-relevant inflation.*

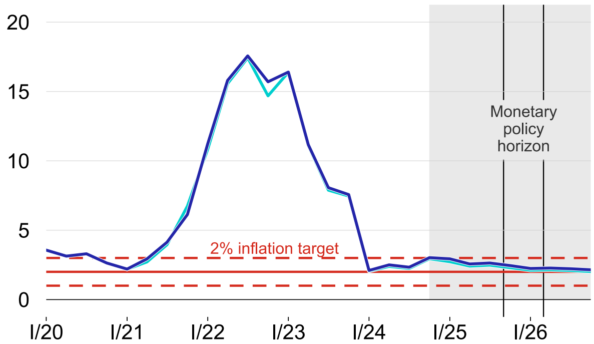
respectively. Excise duty on tobacco and alcohol will go up by a further 5% at the start of 2026. Headline inflation will therefore be slightly above monetary policy-relevant inflation over the entire outlook (see Chart III.8).

Like headline inflation, monetary policy-relevant inflation will be close to the central bank's 2% target over the monetary policy horizon, i.e. in 2025 Q4 and 2026 Q1 (see Chart III.8).

Chart III.8

Headline and monetary policy-relevant inflation will both be close to the 2% target at the monetary policy horizon

headline and monetary policy-relevant inflation; in %



COMPARISON WITH THE PREVIOUS FORECAST: Price developments

		2024	2025	2026	
Consumer prices	y-o-y changes in %	**2.5**	**2.6**	**2.2**	The inflation forecast has shifted upwards mainly because of stronger food price inflation.
	pp	(0.2)	(0.7)	(0.2)	
Administered prices	y-o-y changes in %	**6.2**	**1.6**	**2.0**	The slightly lower outlook for administered prices for next year is due to a larger reduction in the commodity component of housing-related energy prices.
	pp	(0.4)	(-0.4)	(0.1)	
Core inflation	%	**2.5**	**2.5**	**2.2**	The core inflation forecast remains almost unchanged over the outlook horizon.
	pp	(0.0)	(0.1)	(-0.1)	
Food prices (incl. alc. bev. and tobacco)	y-o-y changes in %	**0.9**	**3.8**	**2.2**	Food price inflation will be markedly higher in 2025 than in the summer forecast due to the observed outcomes and stronger growth in import prices of some food commodities.
	pp	(0.8)	(2.4)	(0.4)	
Fuel prices	y-o-y changes in %	**-0.7**	**-3.9**	**-0.2**	The fuel price forecast for next year has shifted upwards, with the somewhat weaker koruna expected in the new forecast outweighing a lower oil price outlook.
	pp	(-1.4)	(0.9)	(2.4)	

Note: Changes compared to the previous forecast in brackets (a green label indicates an increase in value and a red label a decrease)

IV. MONETARY POLICY

At its November monetary policy meeting, the CNB Bank Board lowered the two-week repo rate to 4%, the discount rate to 3% and the Lombard rate to 5%. The Bank Board assessed the risks and uncertainties of the outlook for the fulfilment of the inflation target as modestly inflationary overall. Higher-than-expected inertia in services inflation is an inflationary risk. Potential excessive growth in total public sector spending would lead to a risk of the state budget having an inflationary effect. Increased wage demands in the private and public sector are an additional upside risk. An inflationary risk in the longer term is a potential acceleration of money creation in the economy stemming from a significant recovery in lending activity, especially on the property market. By contrast, a downturn in global economic activity and weaker German – and hence Czech – economic output are a significant downside risk to inflation. This is also reflected in the outlook for further rate cuts by major central banks. Consistent with the baseline scenario of the autumn forecast is a continued decline in short-term market interest rates initially, followed by broadly stable rates from mid-2025 onwards. Their path reflects falling foreign interest rates, fading cost pressures and a closing positive gap in mark-ups.

Consistent with the forecast is a continued decline in short-term market interest rates initially, followed by broadly stable rates from mid-2025 onwards

The autumn forecast implies a further decline in short-term market interest rates over the next few quarters (see Chart IV.1). Interest rates will approach the estimated monetary policy-neutral level in mid-2025 and stay there in 2026. Although growth in costs will remain slightly elevated for the rest of this year and in the first half of next year due to persisting higher-than-usual wage growth, stagnating labour efficiency growth and rising prices of imports, this will not reverse the need to ease monetary policy further. The inflationary effect of the growth in costs will be partly offset by a decline in firms' profit margins, which will continue to dampen growth in prices, and inflation will thus fall to close to the 2% target at the monetary policy horizon. Continued monetary easing by the ECB is also creating room for a decline in domestic interest rates.

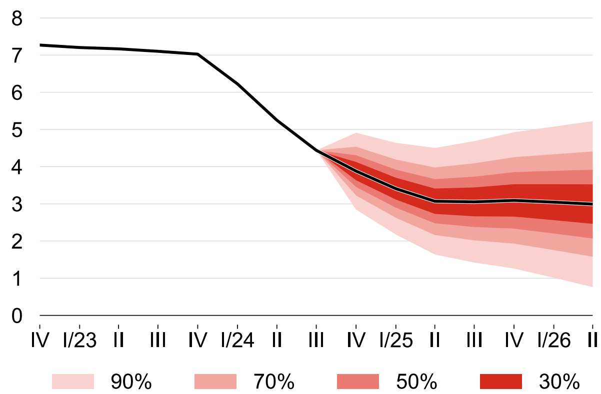
The koruna has been slightly volatile in recent months

The koruna erased part of its previous losses in August after an unsurprising interest rate cut of 25 basis points and the following press conference given by the CNB Governor. It then appreciated until the start of September. The trend reversed towards depreciation in October due to a strengthening dollar and rising global risk aversion. The koruna did not react strongly to the CNB meeting in late September. The average exchange rate in Q3 was CZK 25.2 to the euro, representing a year-on-year depreciation of 4.3%. The koruna fluctuated around CZK 25.3 to the euro in the second half of October.

Chart IV.1

Consistent with the forecast is a continued decline in short-term market interest rates initially, followed by broadly stable rates from mid-2025 onwards

3M PRIBOR in %; confidence interval



***The confidence intervals of the forecasts** for key macroeconomic variables reflect the predictive power of past forecasts. They are symmetric and linearly widening. In the case of headline inflation, they widen only for the first five quarters and then stay constant. This is consistent with both the past predictive power and the stabilising role of monetary policy.*

***The monetary policy horizon** (normally 12–18 months ahead) is the future time period which the CNB focuses on when making its monetary policy decisions. It reflects the length of the transmission of monetary policy. By targeting inflation at this horizon, the central bank also abstracts from short-term inflation shocks, whose impact monetary policy can control to only a minimal extent.*

The favourable effect of the current account surplus was counteracted to the disadvantage of the koruna by a worse economic outlook and an outflow of equity and debt capital in response to lower expected CNB rates.

The koruna will depreciate very slightly over the outlook horizon

The baseline scenario of the autumn forecast expects the koruna to average CZK 25.3 to the euro in 2024 Q4. The koruna weakens gradually to CZK 25.6 to the euro over the outlook horizon (see Chart IV.2), due mainly to an only gradual improvement in the currently subdued labour productivity amid a falling trade surplus. The weaker koruna over the outlook horizon is also due to a decrease in the equilibrium rate of appreciation of the koruna. Starting from the summer forecast, the assumed year-on-year equilibrium rate of appreciation of the koruna was reduced from 1.5% to 1%.[18] A narrowing interest rate differential vis-à-vis euro rates (see Chart IV.3) will also foster a weaker koruna in the first half of 2025.

The market interest rate outlook is slightly above the CNB forecast

The market outlook for short-term FRA rates moved slightly lower during the summer. The market thus continued to expect the 3M PRIBOR to decline gradually at the one-year horizon (see Chart IV.4). This outlook for 2025 is slightly above the interest rate path in the baseline scenario of the CNB's autumn forecast. Almost all the respondents in the FMIE survey were expecting the 2W repo rate to be reduced by 0.25 pp at the November monetary policy meeting. One respondent was expecting rates to be left unchanged. The analysts expect the CNB's key interest rate to be in the range of 2.5%–4% (median 3%) one year ahead.

On average, the analysts in the FMIE and FECF surveys expect the koruna to be at CZK 25 to the euro or slightly below this level one year ahead (see Table IV.1). Their forecasts thus expect a stronger exchange rate than the central bank's outlook. From the long-term perspective, the analysts expect the koruna to appreciate due to favourable developments in the domestic economy and the interest rate differential vis-à-vis the euro area. If it remains subdued, German economic output could have the opposite effect. The difference between the minimum and maximum expected exchange rate one year ahead in the two surveys is almost CZK 3 to the euro.

The Bank Board's communications before the November meeting were signalling a cautious approach to lowering interest rates

Chart IV.2

The koruna will depreciate very slightly over the outlook horizon

CZK/EUR exchange rate; confidence interval

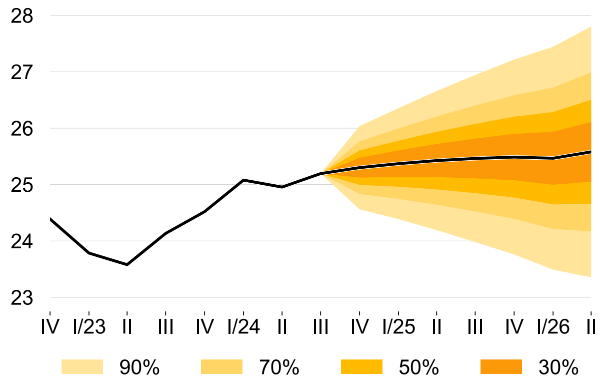


Chart IV.3

The interest rate differential has stabilised vis-à-vis euro rates and has been negative vis-à-vis dollar rates for several months now

pp; differential of Czech money market rates vis-à-vis EUR and USD rates

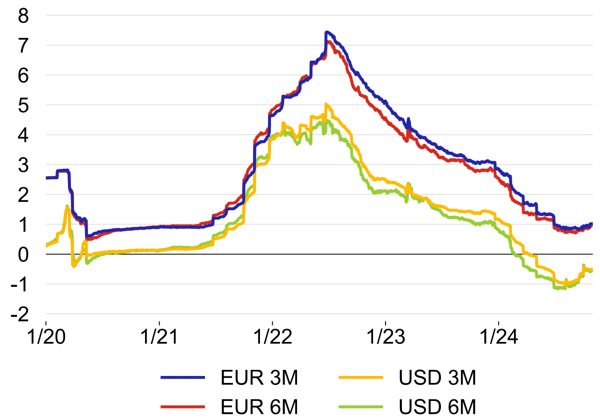
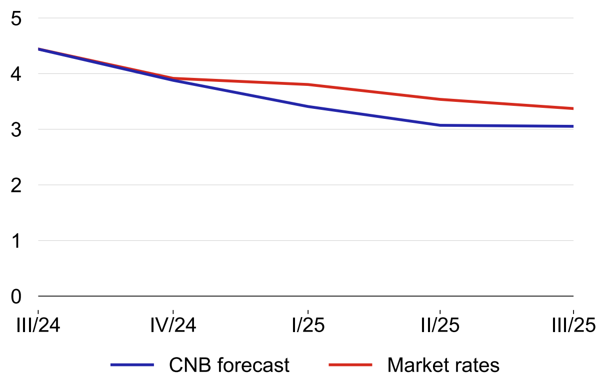


Chart IV.4

The market was expecting rates to be lowered further at the November meeting; the market outlook for next year is slightly above the CNB forecast

3M PRIBOR; FRA in %



Note: Market rates represent for 2024 Q3 the 3M PRIBOR and for 2024 Q4–2025 Q3 the average values of the FRA 1*4, 3*6, 6*9 and 9*12 rates for the last 10 trading days as of 31 October 2024.

18 This adjustment was expertly incorporated into the summer forecast. The autumn forecast was prepared with the aid of the core forecasting model using the reduced equilibrium rate.

Several Bank Board members have said they see room to reduce interest rates further. They have also said that the timing and size of this reduction should be considered. According to some of the Board members, the weak performance of other economies, especially Germany, is fostering lower interest rates. This factor is also slowing the Czech economy. However, the rate reduction process may also be halted, owing to potential inflation risks in the domestic economy. These risks include persisting high inflation in services and, in the longer term, growing activity on the housing market and a higher state budget deficit. It has also been said that inflationary risks currently predominate and that this justifies a cautious approach to lowering rates. Bank Board members also emphasised in their communications that interest rates will remain higher in the longer term than in the previous ten years.

*The **3M PRIBOR market interest rate** is a money market reference rate with a maturity of three months which is closely linked to the CNB's monetary policy rates. The CNB's key rate is the **two-week (2W) repo rate**, paid on commercial banks' excess liquidity as absorbed by the CNB in two-week repo operations. The difference between the 3M PRIBOR and the 2W repo rate fluctuates over time and reflects, among other things, expectations regarding the future path of monetary policy interest rates. This difference currently (before the CNB Bank Board's November monetary policy meeting) stood at −0.2 pp.*

COMPARISON WITH THE PREVIOUS FORECAST: Interest rates and the exchange rate

Chart IV.5

The interest rate path is appreciably lower than in the summer forecast

decomposition of changes in 3M PRIBOR forecast in pp

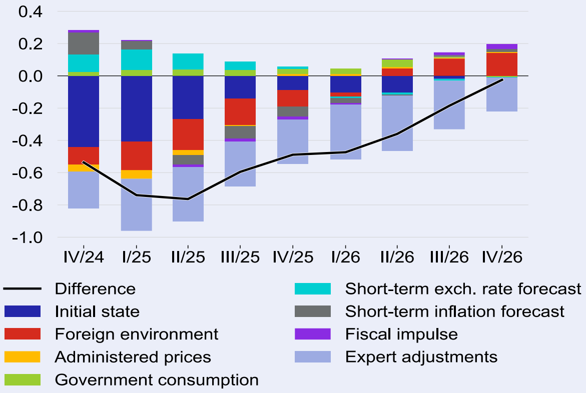
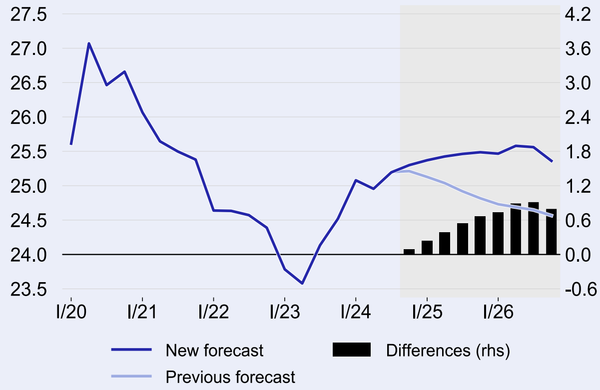


Chart IV.6

The exchange rate forecast has shifted to significantly weaker levels

change in CZK/EUR exchange rate forecast; differences in CZK – right-hand scale



Comparison of the interest rate path with the previous forecast (see Chart IV.5)

- The **initial state** fosters lower rates. This is due to slower wage and GDP growth in 2024 Q3. This effect is partly offset by worse labour productivity this year. The negative contribution of the initial state also reflects the incorporation of a **lower equilibrium rate of appreciation of the koruna exchange rate** into the core forecasting model in a structural way, including a revised interpretation of the koruna's previous effect in the economy. The exchange rate of the koruna observed in the recent past is now seen as stronger, implying tighter monetary conditions in the past. This creates room for a somewhat faster decline in interest rates over the outlook horizon, which will offset the previous restrictive effect of the exchange rate.
- The negative contribution of the **foreign environment** mainly reflects a significantly lower outlook for ECB interest rates compared with the assumptions of the summer forecast.[19] This effect is partly offset by slower expected appreciation of the euro against the dollar.
- The **short-term exchange rate forecast** for 2024 Q4 is set at a slightly weaker level than implied by the core prediction model's interpretation of macroeconomic developments and thus has a slightly upward effect on rates.
- The **short-term inflation forecast** initially fosters slightly higher interest rates for the end of 2024 and the start of 2025. The contribution then turns negative, as the baseline scenario does not expect the higher inflation at the turn of the year – caused by volatile food prices – to propagate further.
- The impacts of the revised outlook for **administered prices, general government consumption** and the **fiscal impulse** are negligible.
- **Expert adjustments** foster lower rates overall. They reflect adjustments fostering slower wage growth and more subdued household consumption due to persisting poor sentiment in the economy. These factors will outweigh the inflationary effect of a more gradual recovery in labour productivity.

Comparison of the koruna exchange rate with the previous forecast (see Chart IV.6)

- The koruna is much weaker than in the summer forecast due to both domestic and foreign factors. A more gradual recovery in external demand and a narrower interest rate differential vis-à-vis the euro area foster a weaker exchange rate from the foreign environment. Factors with the same effect in the domestic economy include a slower improvement in labour efficiency and lower domestic economic growth due to worse household and business sentiment.
- A weaker koruna is also fostered by the incorporation of a lower pace of appreciation into the forecasting model in a structural way, including a revised interpretation of the koruna's previous effect in the economy towards greater overvaluation.

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19 The market outlook itself expects a more marked drop in ECB rates than assumed by the forecast due to concerns of continued adverse economic developments in the euro area. The forecast thus includes an expertly adjusted path that takes into account ECB communication signalling a slower decline in interest rates.

Money market rates are declining, while rates with longer maturities have been fluctuating

PRIBOR rates have been falling gradually this year in response to the lowering of the CNB's key interest rates. The slope of the money market yield curve is negative, due to expectations that monetary conditions will continue to ease in this way. Domestic rates with longer maturities (over 2Y) have largely followed rates on foreign markets (see Chart IV.7). Long-term foreign rates have been mostly declining since June, owing to expected cuts in key ECB and Fed interest rates. The downward trend was interrupted by escalating tensions in the Middle East in early October, which were also reflected in the price of oil. Overall, the changes to domestic IRS rates have ranged between −1.6 pp and +0.3 pp at individual maturities since the start of this year. Government bond yields have changed by roughly the same amount. The slightly convex shape of the domestic IRS and government bond yield curves – with a minimum at around 5Y maturity – remained approximately unchanged (see Chart IV.8).

Client interest rates are following financial market rates

The transmission of the cuts in the CNB's key interest rates is rapid in the segment of loans to non-financial corporations, which follow the 3M PRIBOR money market rate with no lag.[20] The rate on new koruna loans to corporations has thus dropped by 2.7 pp overall to 6.0% in September since the CNB's key rates were lowered last December. Following a decline, the difference compared to the rate on euro-denominated corporate loans is around 1 pp. On the other hand, the rate on new loans for house purchase has not changed much in recent months. Since the end of last year, it has fallen by 0.5 pp to 4.9% in September (see Chart IV.9). The rate on housing loans reacts to financial market rates with longer maturities, usually with a lag of four months. Market rates with longer maturities declined from July to September, and unless their trend reverses significantly, this creates room for a decrease in mortgage rates in the period ahead.

Interest rates on deposits also respond fairly quickly to the decline in monetary policy and market rates. The rate on new deposits with agreed maturity has fallen by 2.5 pp since last December to 3.7%. Real interest rates remain positive.

Growth in loans to corporations has been relatively subdued so far, while growth in loans to households has risen

Growth in corporate loans slowed to 3.8% year on year in 2024 Q3. The lower growth reflected base effects,

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20 The transmission of monetary policy rate cuts to client interest rates was discussed in the box How do client rates on koruna loans change in response to changes in market rates? in the Summer 2024 MPR.

Chart IV.7

The downward trend in domestic interest rates with longer maturities has halted in recent weeks

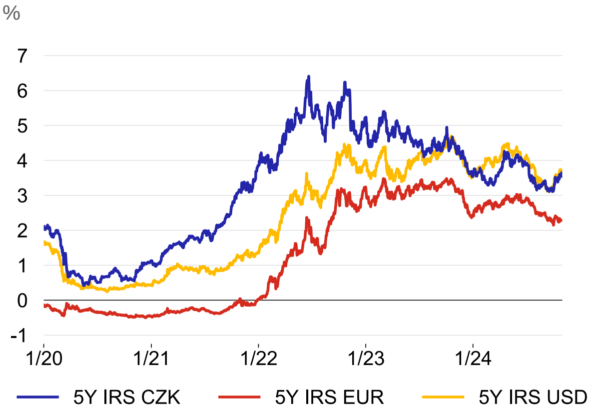


Chart IV.8

The yield curve has stopped moving lower; it remains slightly convex

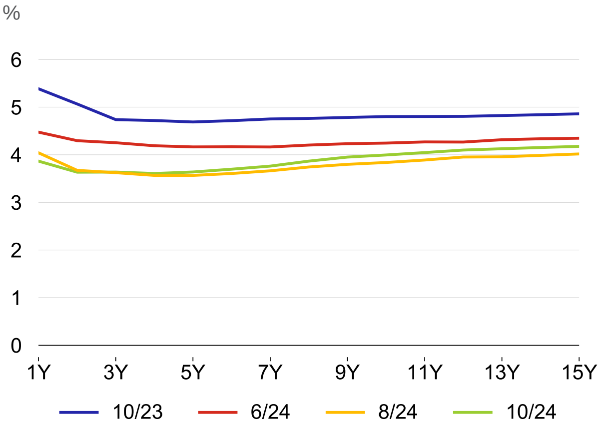
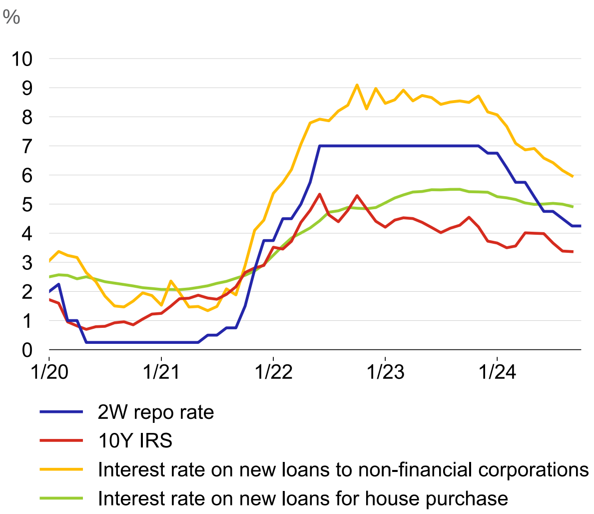


Chart IV.9

Interest rates on loans to corporations decreased further, while those on loans for house purchase were broadly unchanged



but a recovery in loans is now visible in quarter-on-quarter terms. The growth in corporate loans was due mainly to foreign currency loans and this time also to koruna loans. The volume of new koruna loans increased amid a decrease in domestic interest rates. The share of foreign currency loans in total loans to corporations stayed close to 52%. According to the Bank Lending Survey, corporations' demand for loans went up slightly in Q3 following previous declines. This was due mainly to higher financing of fixed investment and working capital and – for the first time since 2021 – lower interest rates. However, according to some banks, firms remain cautious, as uncertainty about the economic outlook and new orders is affecting their motivation to invest more in fixed assets. According to the forecast, growth in loans to corporations will rise (see Chart IV.10) in response to a gradual decline in interest rates in the domestic economy and abroad, and to faster economic growth.

Growth in loans to households for house purchase rose to 4.1% in Q3. Genuinely new mortgages continue to grow strongly due to higher activity on the housing market accompanied by a rise in house prices and a slight fall in mortgage rates. The higher demand in August also reflected an amendment to the law governing the conditions for early repayment of mortgages. This effect dropped out in September and genuinely new mortgage loans returned close to CZK 20 billion. According to the Bank Lending Survey, this represented a five-quarter-long trend of broad-based growth in demand for loans. According to the forecast, growth in housing loans will rise further this year due to growing demand for mortgage loans (see Chart IV.10).

Growth in consumer credit rose to 9.1% in Q3. New loans suggest higher demand in this credit market segment as well, primarily because of a slight increase in consumption expenditure and stabilisation of household sentiment. According to the forecast, growth in consumer credit will start to slow during 2025.

Growth in the quantity of money in the economy was flat

The annual growth rate of M3 was little changed in Q3, reaching 5.5% in September (see Chart IV.11). The contribution of general government financing to M3 growth increased to 1.6 pp in September. It was above its long-term average (0.2 pp in 2010–2019). The contribution of loans to the private sector was 3 pp, remaining below the long-term average (4 pp) for now. On the other hand, the annual growth rate of net foreign assets declined.

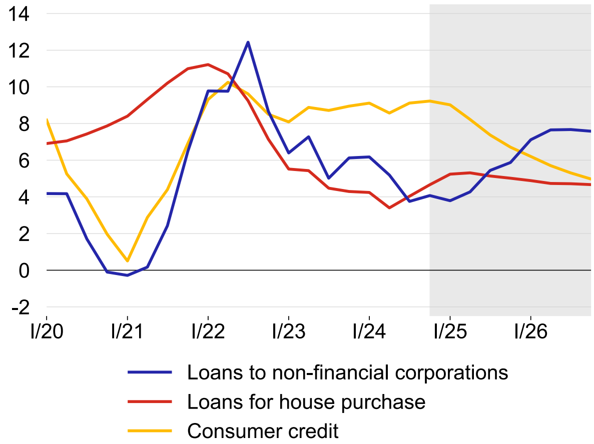
Inflation expectations of firms remain above the 2% target

The available indicators are signalling that inflation expectations are falling gradually. However, they remain above the 2% target, especially in the case of

Chart IV.10

Growth in loans to households for house purchase and especially in loans to corporations will pick up pace

annual rates of growth in %

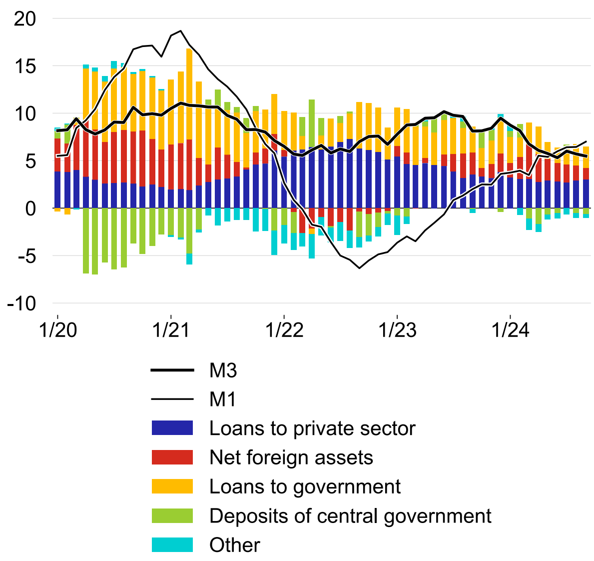


Note: The annual rates of growth in loans to corporations and households until March 2024 were affected by the purchase of the loans of Sberbank CZ by Česká spořitelna in April 2023.

Chart IV.11

The contribution of general government financing to M3 growth increased in Q3

annual rates of growth in %



firms. According to a joint survey conducted by the Confederation of Industry and the CNB, the inflation expectations of non-financial corporations one year ahead declined to 3.3% in September (see Table IV.1). They are only slightly higher three years ahead (see Chart IV.12). Firms are also asked about the prices of their main inputs (commodities, materials, energy, etc.) one year ahead. This forward-looking indicator was approximately flat at 4.3% in September. The European Commission's business survey shows that the share of firms expecting the prices of their products and services to increase in the near term remains low.

Concerns about growth in the price level persisted among Czech households. The gradual (roughly two year-long) decline in inflation perceived by domestic households in the European Commission survey from all-time highs came to a halt. The inflation rate expected one year ahead rose slightly during the summer but remains low from a long-term perspective (see Chart IV.13). According to the CZSO's October business survey, too, consumers' concerns about rising prices increased slightly. However, the outlook for their financial situation improved somewhat.

Inflation expected by financial market analysts is just above the CNB's 2% target at both the one-year and three-year horizons.

The risks of the forecast are modestly inflationary overall

Higher-than-expected inertia in services inflation is an inflationary risk. Potential excessive growth in total public sector spending would lead to a risk of the state budget having an inflationary effect. Increased wage demands in the private and public sector are an additional upside risk. An inflationary risk in the longer term is a potential acceleration of money creation in the economy stemming from a significant recovery in lending activity, especially on the property market. By contrast, a downturn in global economic activity and weaker German – and hence Czech – economic output are a significant downside risk to inflation. This is also reflected in the outlook for further rate cuts by major central banks.

Heightened geopolitical tensions related to the ongoing war in Ukraine and the conflicts in the Middle East remain a general uncertainty of the forecast. The impacts of the outcome of the US presidential election and its implications for the exchange rates of risky currencies, which include the Czech koruna, are also uncertain.

Greater inertia in observed services inflation is an inflationary risk

The baseline scenario of the autumn forecast expects inflation to be at around 3% over the next few months. The deviation of inflation from the 2% target will thus remain elevated for some time. This may lead to growth

Table IV.1

Analysts' inflation expectations at the three-year horizon are slightly above the inflation target; those of firms are above 3%

sample of approximately 18 analysts and 150 corporations; 1Y horizon; annual percentage changes unless otherwise indicated

	6/24	7/24	8/24	9/24	10/24
FMIE:					
CPI	2.2	2.1	2.1	2.2	2.2
CPI, 3Y horizon	2.2	2.1	2.2	2.1	2.2
Real GDP in 2024	1.3	1.3	1.0	1.0	1.0
Real GDP in 2025	2.7	2.6	2.6	2.5	2.4
Nominal wages in 2024	6.8	6.8	6.9	6.7	6.7
Nominal wages in 2025	5.4	5.4	5.4	5.5	5.5
CZK/EUR exchange rate (level)	24.6	24.7	24.8	24.8	24.6
2W repo rate (%)	3.5	3.4	3.4	3.4	3.3
1Y PRIBOR (%)	3.6	3.4	3.4	3.3	3.3
Corporations:					
CPI	3.8			3.3	
CPI, 3Y horizon	3.7			3.5	
CF:					
Real GDP in 2024	1.3	1.2	1.1	1.1	1.1
Real GDP in 2025	2.7	2.7	2.7	2.6	2.6
Nominal wages in 2024	6.2	6.6	6.8	6.7	6.5
Nominal wages in 2025	5.4	5.4	5.5	5.6	5.5
CZK/EUR exchange rate (level)	24.9	24.9	24.9	24.9	25.0
3M PRIBOR (%)	3.4	3.4	3.5	3.5	3.4

Chart IV.12

Inflation expectations declined further among non-financial corporations at the three-year horizon but remain above the 2% target

sample of approximately 18 analysts and 150 corporations; %

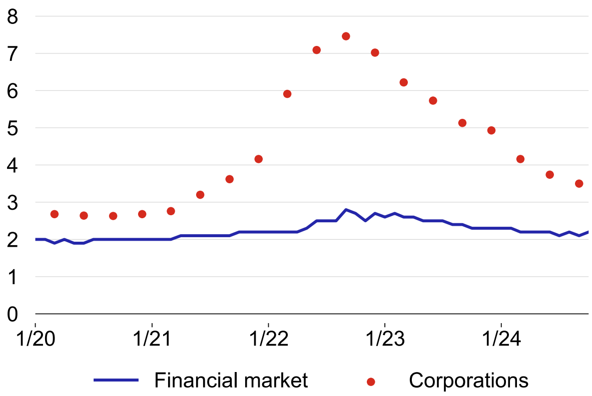
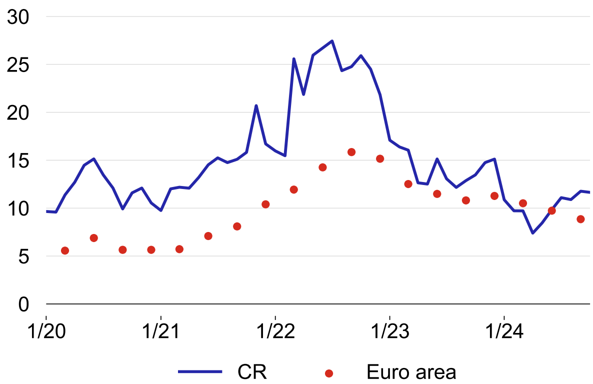


Chart IV.13

The inflation expectations of Czech and euro area households fell only marginally compared to the end of last year

households' inflation expectations in next 12 months according to European Commission Business and Consumer Survey; sample of approximately 1,000 households for the Czech Republic; in %



in inflation expectations, reducing the restrictive effect of interest rates (assumed in the baseline scenario), and thus be a source of additional inflation pressures. In an environment of even only temporarily higher inflation, retailers and service providers may resort to greater-than-expected repricing of services in an effort to keep their profit margins higher for longer. A scenario considering higher growth in services prices next year due to slower closure of the gap in mark-ups has been constructed to illustrate this risk.

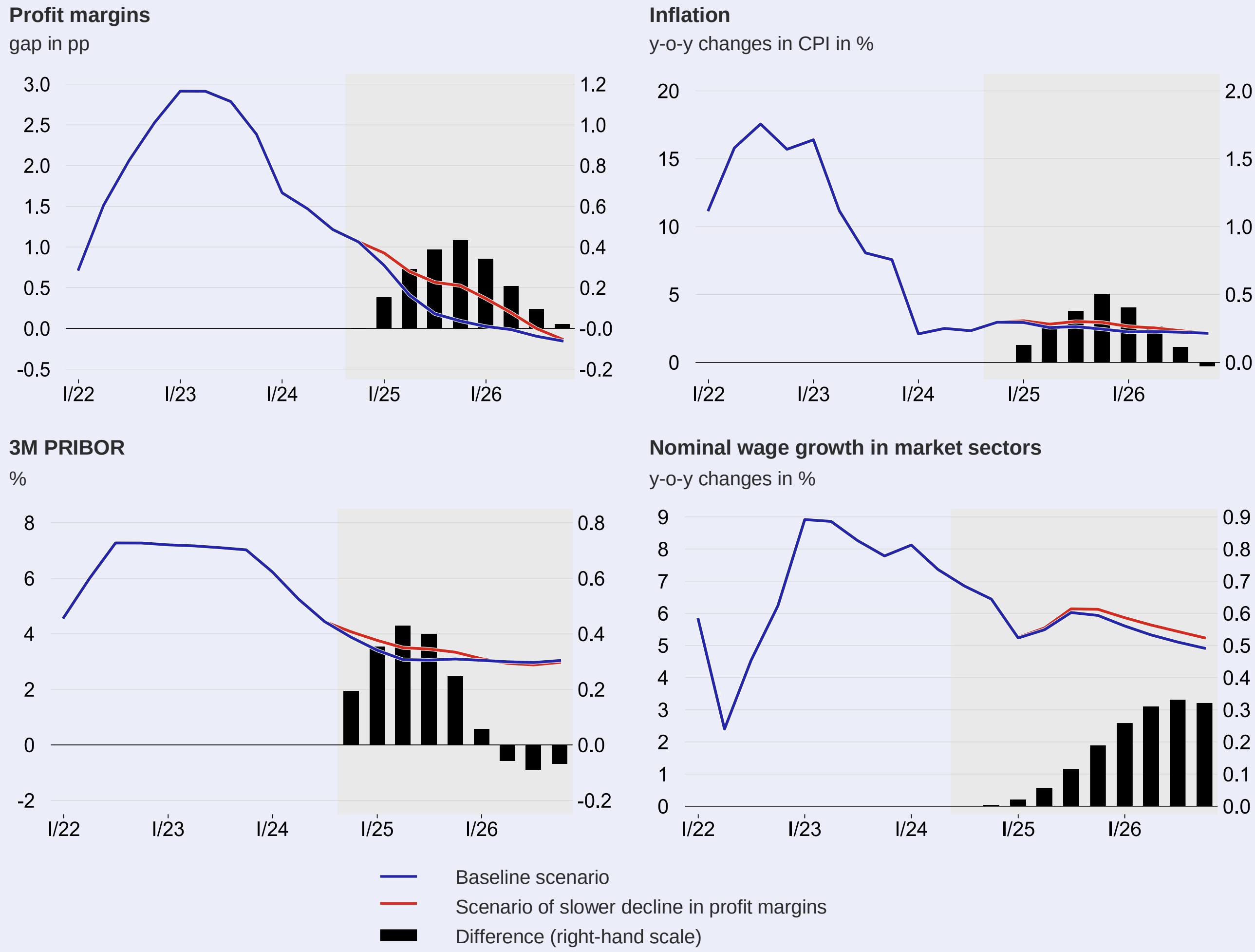
Scenario of a slower decline in profit margins

This scenario describes a situation where, in an environment of elevated inflation in late 2024 and early 2025, service providers resort to greater repricing in an effort to keep their profit margins higher for longer. This is reflected in 1.5 pp higher annualised quarterly services inflation in each quarter of next year compared with the baseline scenario of the forecast. As a result, year-on-year headline consumer price inflation is 0.5 pp higher than in the baseline scenario at the end of next year. The central bank reacts to this higher inflation with higher interest rates (a more moderate decline) than in the baseline scenario at the end of this year and throughout 2025. In spite of that, the higher inflation is partly reflected in faster nominal wage growth compared with the baseline scenario.

Chart IV.14

The central bank reacts to higher inflation next year caused by a slower decline in profit margins with higher interest rates already at the end of this year

comparison of baseline scenario with scenario of slower decline in profit margins



A potential disequilibrium on the demand side of the property market is an inflationary risk in the longer term

Demand for new housing loans, which has been rising across the board for five quarters according to the Bank Lending Survey, remains solid due to continued expected growth in house prices, stabilisation of consumer sentiment and a gradual fall in interest rates, even though the decline in mortgage rates has halted temporarily in recent months. Lower flexibility can be seen on the supply side of the housing market, with the numbers of apartment starts and completions currently falling year on year.[21] Any growth in the price disequilibrium on the housing market could greatly increase distortions across the economy, create an underlying inflationary environment and have a significant lagged effect on consumer prices.

The relevance of this risk is further highlighted by recent developments in asking prices of apartments. Their quarter-on-quarter growth has been rising since the start of 2024 and exceeded 13% in annualised terms in Q3 (see Chart IV.15). In recent months, the volume of genuinely new mortgages in real terms has also been around that in the pre-Covid period, which was characterised by a rapid recovery of the housing market. The Inflation and Monetary Policy Risks Scoreboard is also currently indicating an inflationary risk relating to house prices (see below).[22]

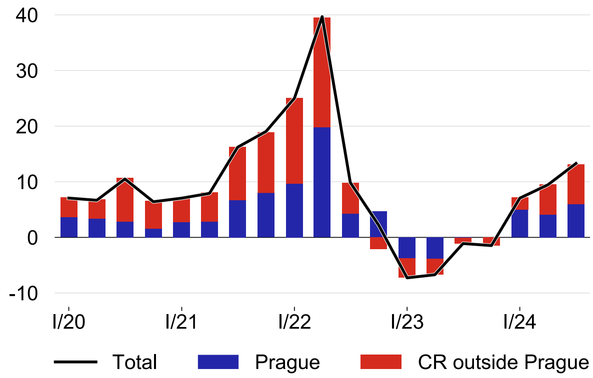
A downturn in global economic activity or a slower economic recovery in the euro area and a related faster decline in ECB rates are a significant downside risk

The baseline scenario of the autumn forecast assumes that economic growth in the effective euro area will pick up in the course of next year, especially as the economic headwinds in Germany gradually subside. However, leading indicators of the German economy do not bode well, so the recovery in the euro area may be slower than assumed in the baseline scenario. Weaker economic activity would in turn be reflected in weaker inflation pressures and a faster decrease in ECB interest rates than assumed in the forecast.[23] Overall, this could lead to lower inflation and interest rates in the Czech economy, too. A scenario simulating the potential impacts of an economic downturn in the

Chart IV.15

Growth in the asking prices of apartments has been rising since the start of 2024

apartment asking prices; q-o-q changes in %; contributions in pp; annualised



Note: Prague accounts for roughly 55% and the rest of country for around 45% of the number of apartments on offer in the Czech Republic.

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21 According to CZSO data, apartment starts were 11.3% lower and apartment completions 19.9% lower in August than a year earlier.

22 House prices in the broader context, supply and demand on the housing market and the effect of monetary policy on house prices are discussed in more detail in the Appendix at the end of this Report.

23 The baseline scenario of the forecast assumes an expertly adjusted path of the market outlook for foreign interest rates, which takes into account ECB communication signalling a slower decline in interest rates. For details, see the blue information box in section I.

euro area on the domestic economy has been constructed to illustrate this risk. The scenario assumes that cyclical factors initially prevail and that structural causes later gain in importance. The latter have the supply-side nature of a fall in productivity (e.g. European car makers lagging behind in electrification, strict EU standards, lower rates of innovation, and a complex and opaque regulatory environment) and are conversely inflationary.

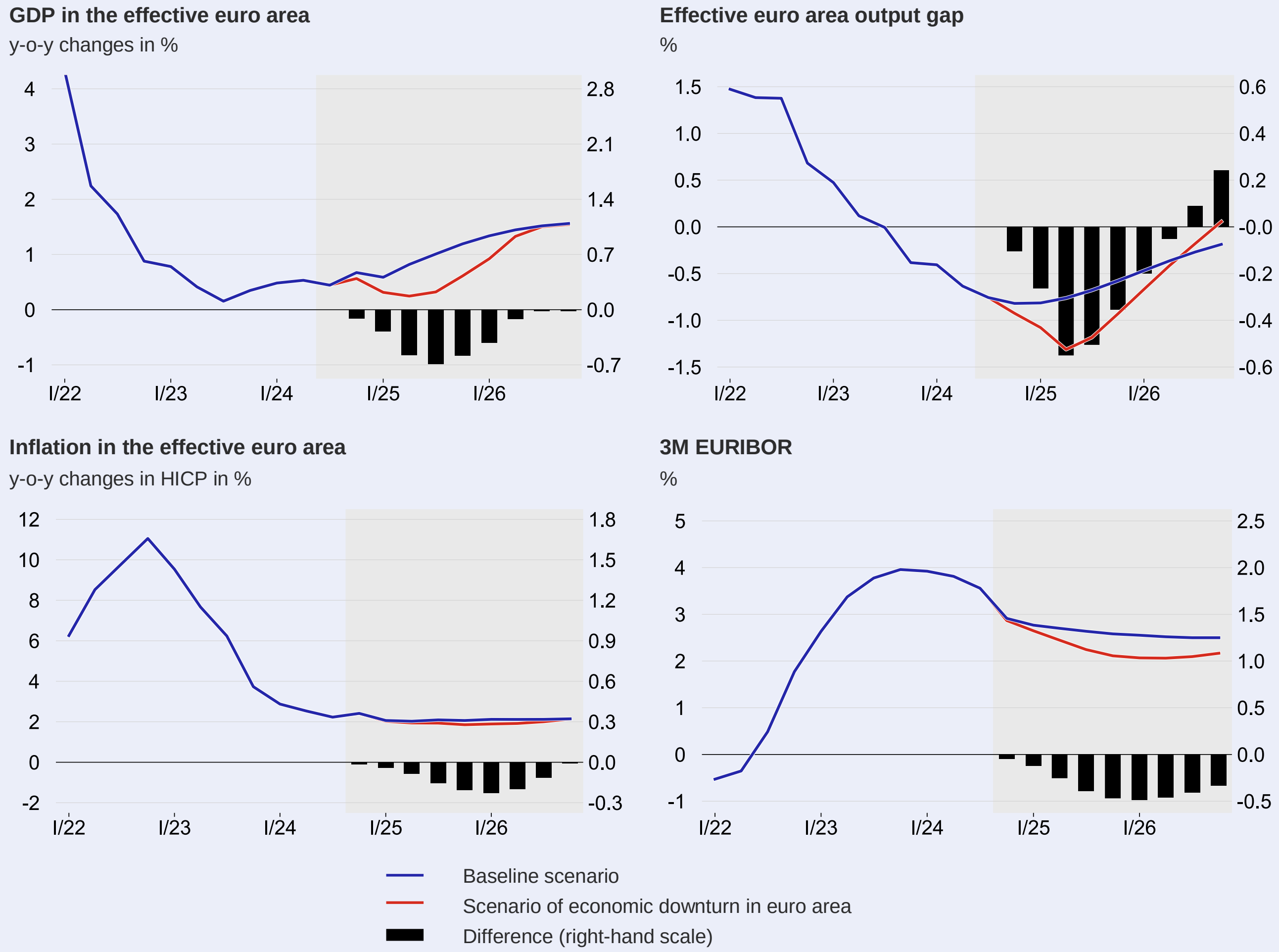
Scenario of an economic downturn in the euro area

One of the risks of the autumn forecast is the euro area interest rate outlook and the still fragile economic growth in many euro area countries, and especially in Germany. This is reflected in differences in opinion on the ECB's future monetary policy. While the 3M EURIBOR market outlook has moved noticeably lower since the previous forecast, the ECB's communication on the future course of monetary policy, on which the CNB's forecast is based, indicates a somewhat higher interest rate path than the market outlook. Therefore, the global NiGEM model was used to construct an alternative euro area outlook consistent with a 3M EURIBOR market outlook that is lower than in the baseline scenario (see Chart IV.16).

Chart IV.16

Subdued economic growth in the euro area is reflected in lower inflation and leads to a faster decline in ECB interest rates

comparison of baseline scenario with scenario of economic downturn in euro area



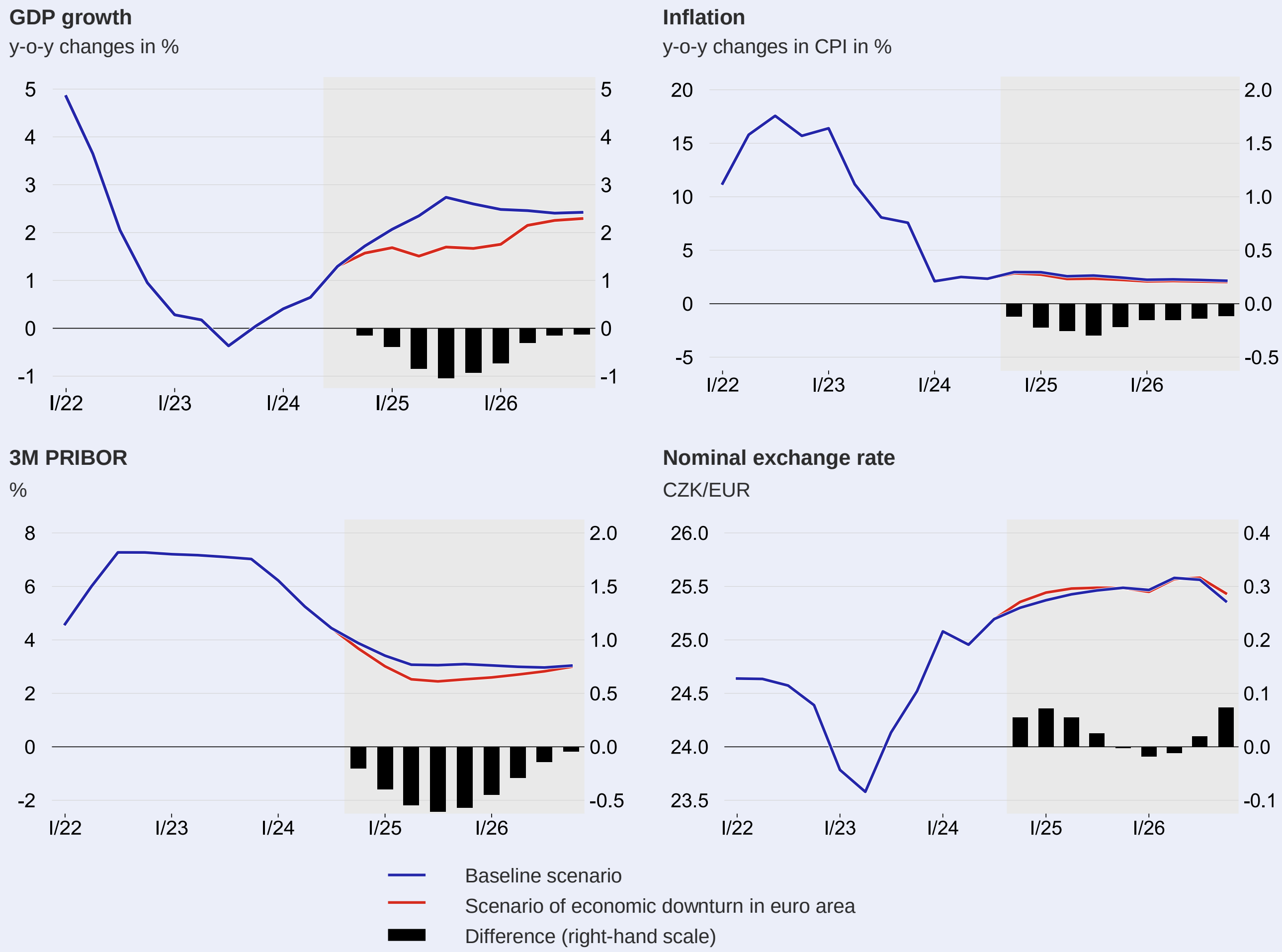
The simulation assumes a deeper cyclical slowdown over the entire forecast horizon than in the baseline scenario, reflecting lower private consumption across all major Czech trading partners in the euro area, and especially in Germany. Beyond this negative demand shock, the scenario also assumes gradually increasing negative structural supply effects in the later quarters of the outlook. These reflect the declining competitiveness of European industry, which – in addition to the technological lag behind the USA and China – is due to significantly higher production input prices, which will be reflected in a decrease in (the rate of growth of) potential output. Overall, the scenario leads to only slightly lower inflation in the euro area, as the prevailing anti-inflationary negative demand impacts – reflecting a more negative output gap than in the baseline scenario – are partly offset by the inflationary effect of a weaker supply side of the economy. The negative demand and supply impacts together result in a greater downturn in real economic activity in the euro area over the entire forecast horizon.

The slower economic growth in the euro area implies a significantly lower outlook for domestic economic activity than in the baseline scenario. Domestic economic growth will therefore be 0.8 pp lower next year than assumed in the autumn forecast. In 2026, the deviation will decrease to 0.3 pp. The more subdued demand pressures from the foreign and domestic economy are reflected in rather lower domestic inflation. In response to this, along with a lower outlook for ECB interest rates, domestic monetary policy rates are lowered more forcefully than in the baseline scenario to below their neutral level. The koruna is weaker in the following quarters due to lower external demand.

Chart IV.17

An economic downturn in the euro area leads to a need for a faster decline in domestic interest rates

comparison of baseline scenario with scenario of economic downturn in euro area



There is increased uncertainty in the domestic economy about wage growth

The short-term forecast expects year-on-year growth in the total average wage to have been 6.1% in 2024 Q3.[24] However, this assumption is subject to data uncertainty related to legislative changes (such as the introduction in July of mandatory registration of all employees working on the basis of agreements to complete a job) and the increased volatility of monthly wage indicators during the summer months. Any deviation of the short-term forecast from the actual figures would lead to a reassessment of the pace of decline in wage growth next year as well.

Beyond the scope of the forecast, the Inflation and Monetary Policy Risks Scoreboard is also identifying several upside risks to inflation

While the Scoreboard is indicating an easing of inflationary risks in the area of the government deficit compared to last year, this area continues to be assessed as high risk, with a worsening trend in the course of this year. The consolidation package is offset by growth in spending related to the elimination of flood damage and the worse deficit last year after the autumn general government deficit and debt notifications. The expected deficit this year is thus very close to the reference value of the Maastricht convergence criterion of 3% of GDP. The persisting deficit also implies a still elevated contribution of general government financing to M3 growth (see Chart IV.11), which could lead to the emergence of an underlying inflationary environment in the domestic economy.[25]

The property price indicator, which reflects the annualised quarter-on-quarter change in the House Price Index, saw a shift in risk from neutral to inflationary in 2024 Q2. The property price gap is also still assessed as slightly inflationary. In addition, the Scoreboard is indicating persisting slightly elevated inflationary risks in the case of unobserved long-term inflation and the anchoring of long-term inflation expectations.

By contrast, the financial conditions index for the euro area continues to point almost exclusively to lower inflation. It describes financial conditions in the euro area as being tighter relative to their long-term level. The variables entering the index include higher central bank interest rates and a widening of the spread between short- and long-maturity bonds.

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24 The average wage growth figure for 2024 Q3 will not be published until 4 December 2024, i.e. more than a month after the closing date of the autumn forecast.

25 The contribution of general government debt, including the release of central government deposits, to M3 growth averaged 1.9 pp from January to September 2024, as against 0.2 pp in 2010–2019.

The long-observed weakening of inflationary risks persists in domestic labour market indicators.

Monetary conditions will be broadly neutral at the start of next year and will then start to be slightly expansionary due to the exchange rate component

The deviations of ex ante[26] real interest rates and the real exchange rate from their equilibrium levels enter the real monetary conditions index (RMCI).

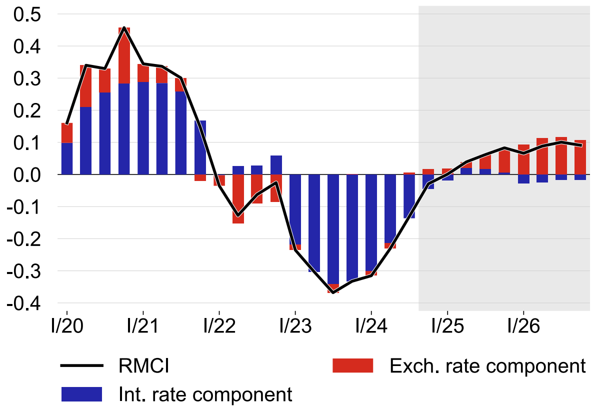
The interest rate component of the monetary conditions is gradually becoming less restrictive and will have a broadly neutral effect at the start of 2025. The expansionary effect of the exchange rate component of the real monetary conditions will strengthen gradually in the course of next year (see Chart IV.18).

Overall, the real monetary conditions are indicating a roughly neutral effect of monetary policy at the start of next year. This will ensure fulfilment of the inflation target at the monetary policy horizon.

Chart IV.18

The restrictive effect of the real monetary conditions is rapidly easing

real monetary conditions index (RMCI); positive (negative) values correspond to easy (tight) monetary conditions



26 From the Summer 2024 MPR onwards, the equilibrium real rate in the interest rate component of the RMCI is set at 1%. The modification was made in order to align this empirical model with approaches related to the g3+ core forecasting model and the theoretical foundations set out in Hlédik, T., Vlček J. (2018): Quantifying the Natural Rate of Interest in a Small Open Economy – The Czech Case. In the original RMCI calculation, the long-term average real rate of around −0.1% was used.

APPENDIX The housing market and house prices in the Czech Republic

Following a decline in 2022, activity on the housing market is on the rise again and is being accompanied by surging house price growth. Property plays a major role in the Czech economy. House price disequilibrium can greatly reduce resource allocation efficiency, exacerbate the imbalances in society and, with a lag, affect consumer price inflation beyond the narrow imputed rent price index itself. This appendix examines house prices in the broader context, supply and demand on the housing market and the effect of monetary policy on house prices.

House prices rose sharply in the period of 2015–2022 (see Chart 1). They peaked during the Covid-19 pandemic and then fell slightly. However, they started to go up again this year. Residential property prices (as measured by the House Price Index, HPI) increased by 4.1% year on year in 2024 Q2 and are 120% higher than in 2015 and 50% higher than in the pre-Covid year 2019. Growth in asking prices of apartments surged to almost 7% in 2024 Q3, with prices exceeding their previous highs. In real terms (adjusted for the CPI), house prices have risen by 44% since 2015.

House prices enter the CPI via imputed rent based on the concept of the prices of the services that dwellings provide to owner-occupiers (the net acquisition approach, NAA). These prices – also referred to as imputed rent – are expressed by the Owner Occupied Housing Price Index (OOHPI). Newly purchased property makes up 15.4% of imputed rent, the remainder being material and other costs associated with individual construction and reconstruction, insurance costs and so on. Given the weight of imputed rent in the CPI (10.3% this year), prices of newly purchased property account for around 1.6% of the CPI. The aforementioned other costs associated with owning property have a greater weight. For this reason, the contribution of house price growth to inflation has long been very low. As Chart 1 shows, the OOHPI (imputed rent) has been rising much more moderately than either the HPI or the asking price index. A pick-up in the OOHPI can be seen in 2021 and early 2022, mainly due to rising prices of building work and materials. The experimental inclusion of existing property transactions (CPIH[1]) would lead to an increase in inflation relative to the CPI of around 1 pp on average between 2015 and 2020 and 2 pp in 2021 (see Chart 2).

Chart 1

House prices started to go up again this year

2010 index = 100; source: CZSO

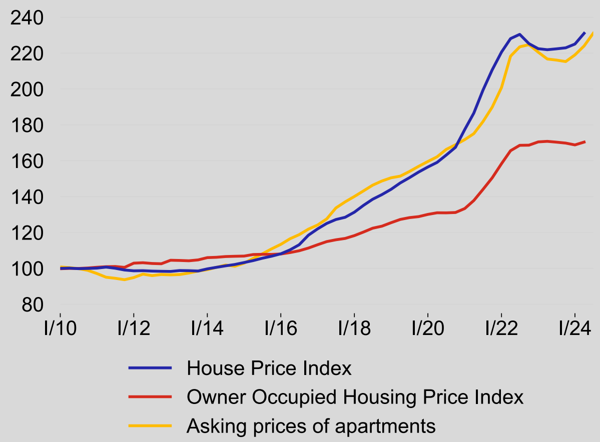
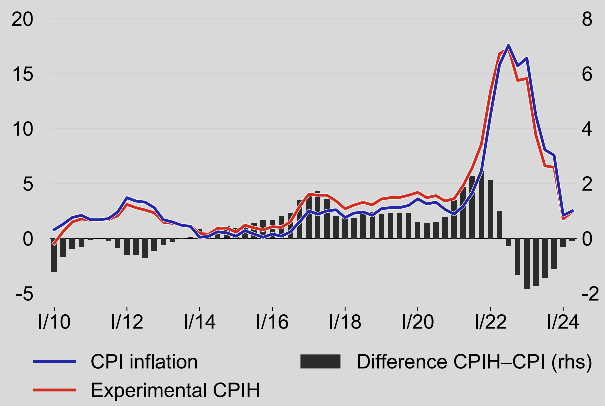


Chart 2

The weight of house prices in inflation is low; given a hypothetical increase in the weight, inflation would have been higher in the past

y-o-y change in %; difference in pp; source: CZSO



House prices (the HPI) rose faster than consumer prices in the past (see Chart 3). The housing market is to some extent determined by domestic factors, and house prices are correlated with the position of the economy in the business cycle with no lag. Their correlation with the output gap stands at 0.5. In the case of the CPI, the peak correlation with the output gap is lagged by three quarters, with a lower correlation coefficient of 0.3. Taking into account monetary conditions in addition to the output gap, house prices recorded rapid growth in the pre-Covid period amid accommodative monetary conditions and a positive output gap.

Chart 3

House prices recorded rapid growth in the pre-Covid period amid accommodative monetary conditions and a positive output gap

y-o-y change in %; output gap in % of potential output; real monetary conditions index (rhs); source: CZSO; CNB calculation

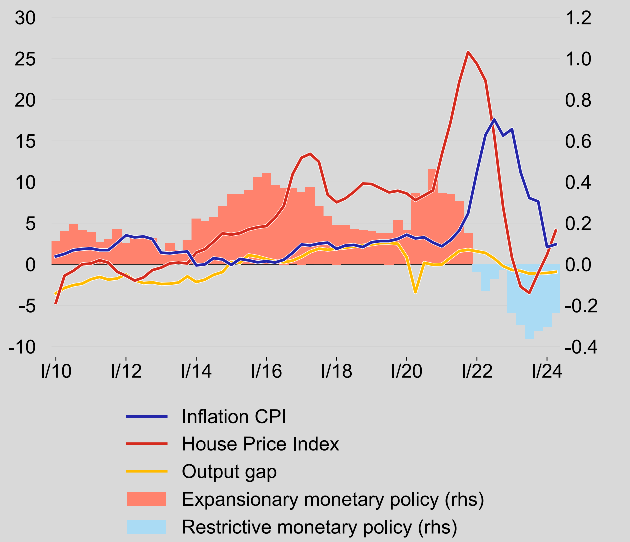
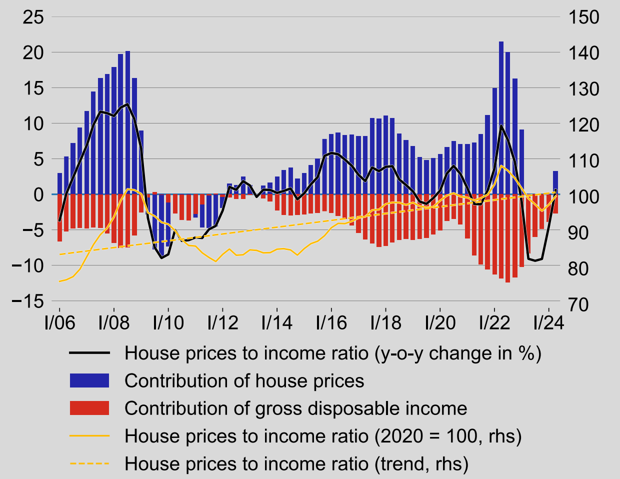


Chart 4

The ratio of house prices to households' gross disposable income is on an upward trend

y-o-y change in %; contributions in pp; 2020 index = 100 and trend (rhs); source: CZSO; CNB calculation



In 2024 Q2, the affordability of owner-occupied housing (OOH) as measured by the ratio of house prices to households' disposable income was just below the 2008 level and at the same level as in 2020, before house prices rose sharply (see Chart 4). The ratio is on a long-term upward trend (indicating a long-term decline in income affordability) due to the Czech Republic's economic convergence towards developed countries. This is because there is a positive relationship between a country's economic level and the OOH costs of its population (see Chart 5). Moreover, due to strong growth in house prices in 2015–2022, which led to the third-largest decrease in housing affordability in the EU (see Chart 6), the Czech Republic is above the line reflecting the estimated relationship (see Chart 5).[2] The ratio of house prices to disposable income in the Czech Republic is thus higher than that implied by its relative economic level.

Chart 5

The ratio of housing costs to income increases as the economic level rises

x-axis: GDP per capita at purchasing power parity; EU27 = 100; y-axis: ratio of housing costs to households' disposable income in % in 2023; R^2 = 0.36; selected European countries; source: Eurostat

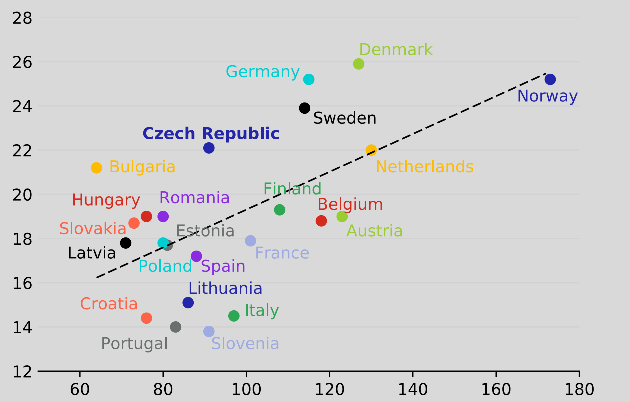
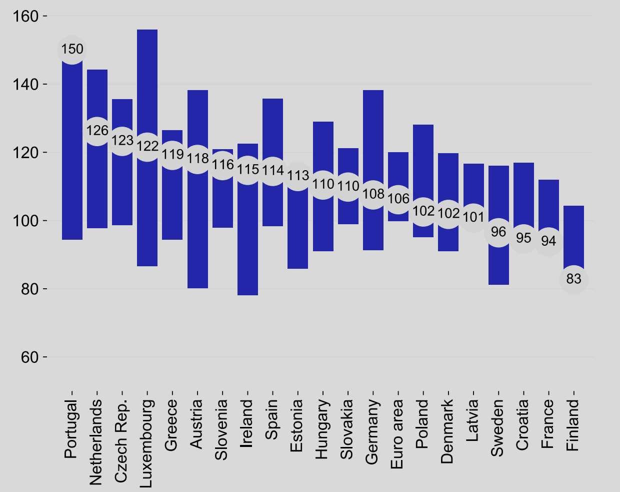


Chart 6

The reduction of housing affordability in the Czech Republic is one of the most significant in Europe

ratio of house prices (HPI) to income in %; 2015 index = 100; minimum and maximum values in 2010 Q1–2024 Q2; actual value in 2024 Q2; selected European countries; source: OECD



One of the reasons for the low affordability of housing in the Czech Republic is an inflexible supply side, as the building permit process is slow and zoning and land use planning do not take sufficient account of housing needs.[3] The Czech Republic meanwhile has a high share of owner-occupied housing. The supply of new apartments has thus been fluctuating close to the 2010 level in recent years (see Chart 7). The numbers of apartment completions and starts even fell by 2% and 5% year on year respectively in the first half of 2024. These year-on-year declines intensified during Q3, even though the numbers of starts and completions increased modestly as developers implemented previously deferred projects. This year, however, the number of building permits issued is at its lowest level since 2010. A particularly large decline in building permits is apparent in Prague.

In contrast to the inflexible supply, demand for housing has been rising for five quarters in a row (see Chart 8). The number of apartments sold in the first half of 2024 was up 13% year and year and was close to the level of 2021 (a successful year in terms of sales). According to the Bank Lending Survey, this is being accompanied by growth in households' demand for housing loans, driven, among other things, by expectations of a continued housing market recovery and related expectations of house price growth. Demand is also being supported by a stabilisation of consumer sentiment in the first half of this year and a modest decrease in mortgage interest rates, with the prospect of a continued decline due to expected further monetary policy rate cuts by the CNB. The deactivation of the DSTI and DTI limits in 2023 and 2024 respectively has also boosted demand for housing.

Chart 7

The supply of housing has decreased recently

numbers of apartments in thousands; annual moving averages; source: CZSO

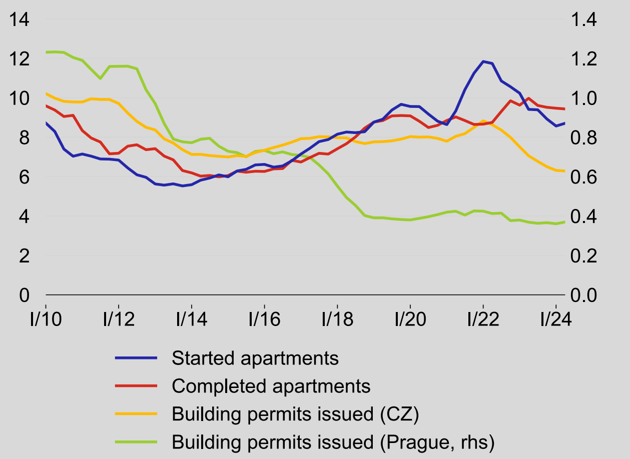


Chart 8

Activity on the housing market is rising and is being accompanied by increased demand for loans

number of apartments sold: y-o-y changes in %; demand for loans: annual moving average of banks' net market shares in % (rhs); source: Dataligence, Bank Lending Survey

New mortgage loans are also now reacting to the economic recovery and the gradual decrease in interest rates (see Chart 9). Their net volume (excluding refinancing)[4] has more than doubled year on year this year in both nominal terms and real terms (adjusted for consumer inflation). Inflation-adjusted housing loan volumes are close to the level of the pre-Covid period, which was characterised by an overheating property market. According to the 2023 Household Finance and Consumption Survey, the percentage of households with a mortgage has increased most of all in the highest (fifth) income quintile.

The household saving rate has meanwhile increased significantly relative to the pre-Covid level, primarily in the form of financial assets (see Chart 10).[5] At the same time, however, almost half of savings are invested in mostly housing-related non-financial assets. According to the 2023 Household Finance and Consumption Survey, financial assets are being accumulated above all by households in the highest income quintile (see Chart 11). Moreover, deposit holdings have fallen least of all in this group of households compared to the others over the past year, so the still large financial buffer in this group of the population may be creating the potential for growth in demand for housing given the assumed decline in interest rates. The interest rate on time deposits at banks reacts quite quickly to CNB monetary policy rate cuts. This will reduce the preference for such deposits.[6] Lower returns on deposits will not only foster growth in consumption, but also motivate people to seek higher returns by investing in riskier financial assets and buying property, which is a popular asset among Czech households.

Chart 9

Mortgage loan volumes have increased markedly in recent quarters

genuinely new loans in CZK billions; CPI-adjusted (2015 = 100); CNB calculation

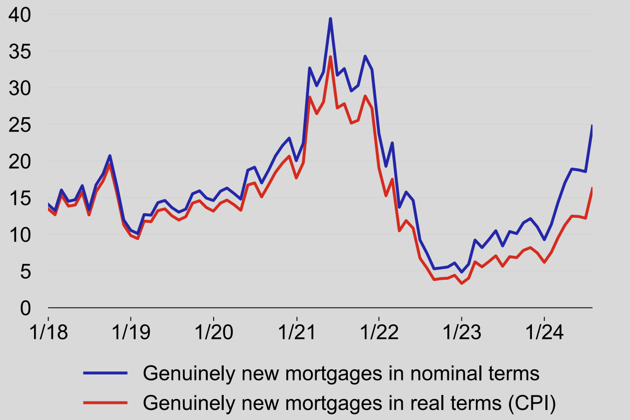
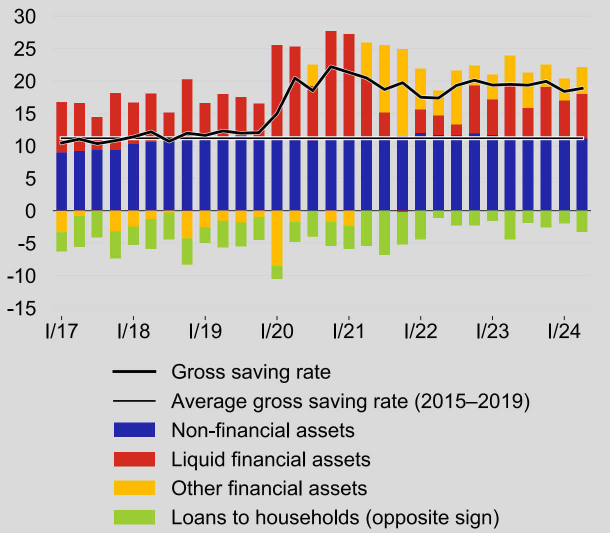


Chart 10

A large part of the new savings created by households since 2020 have been invested in financial assets

ratio of flows to gross disposable income in %; source: CZSO; CNB calculation



Note: Liquid financial assets comprise cash and deposits. Non-financial assets consist of gross capital formation. Other financial assets are calculated as the difference between savings and the aforesaid items.

Chart 11

Higher-income households have relatively large deposit holdings, which could boost growth in demand for property as interest rates fall

ratio of deposits to net annual income in %; median; source: Household Finance and Consumption Survey; CNB calculation

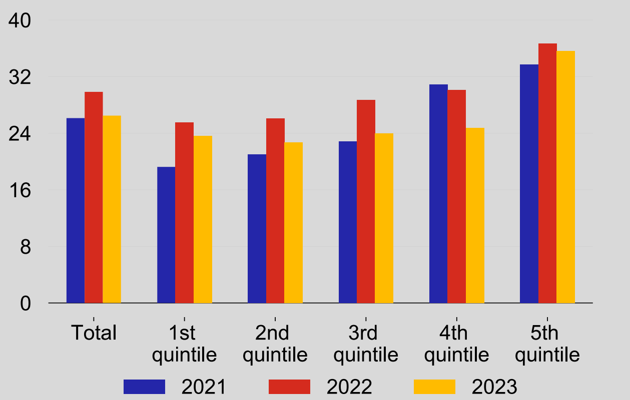
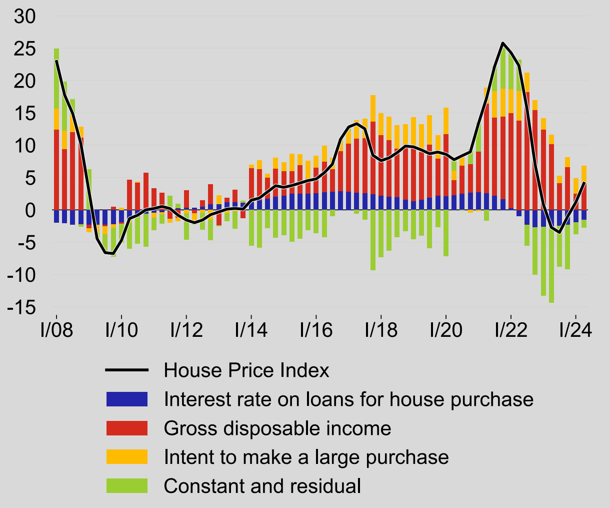


Chart 12

On the demand side, income, sentiment and the interest rate affect property prices in the long term

y-o-y change in HPI in %; contributions in pp; R^2 = 0.70; CNB calculation



According to Šustek and Zapletalová (2023),[7] the growth in house prices in the Czech Republic in the period of 2013–2021 was due primarily to growth – and expected further growth – in real household income. The interest rate was also an important, though less significant, factor alongside income. According to the authors' computations, growth of real household income was responsible for 32 pp of the 78% growth in nominal house prices. A further 15 pp was due to consumer inflation and 20 pp to increasing affordability of mortgage financing, due not only to the interest rate, but also to expected further growth in real household incomes.

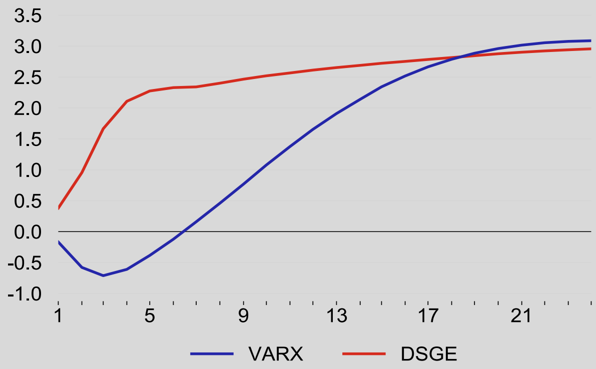
A regression analysis-based method that decomposes house price growth (the HPI) in the period of 2008–2024 offers a similar picture (see Chart 12). The main factor in the long term is nominal disposable income growth, which, for example, accounted for more than half of the growth in house prices in the period of high house price growth (2021). Households' sentiment, or more specifically their willingness to spend on large tangible assets over the next 12 months, contributes in the same direction, but much less so. This follows from the CZSO business cycle indicator as regards the outlook for purchases of furniture and electrical and electronic equipment, which are often connected with house purchases. Low interest rates also contributed to the growth in house prices between 2015 and 2021. Since 2022, by contrast, growth in the average mortgage rate (expressed in terms of the deviation from the neutral level) has been cooling the housing market. Owing to inflexible supply, demand factors have therefore been the prevailing drivers of price changes on the housing market.

The effect of monetary policy on house prices was simulated in more detail using a vector autoregressive model with exogenous variables[8] (VARX) and using the g3+ forecasting model modified to include a housing block (DSGE).[9] Easing the real monetary conditions index by 1 pp causes house prices to increase in both approaches, though with different time distributions (see Chart 13). In the DSGE model, a shock to the monetary conditions will fade away quite quickly due to the monetary policy response consistent with achieving the inflation target. This explains the short-term upward effect on house prices in the first year in particular. By contrast, the econometric VARX model gets going more slowly, with house prices not rising until the middle of the second year. The final effect of the monetary expansion on house prices is close to 3% in both models.

Chart 13

Monetary expansion has a significant effect on house prices

x-axis: quarters; cumulative effect of monetary expansion on house prices in %



The Czech housing market looks to be on the threshold of a new upward phase this year. The latest data are signalling fairly robust quarter-on-quarter price growth, supported by recovering household incomes, rising market rents, gradually falling mortgage rates, a buffer of accumulated capital for buying property among wealthier households, and further expected house price growth. Despite its decreasing affordability, property is a very popular asset in the Czech Republic. Prices of purchased property are included in the consumer price index as part of imputed rent. However, they have a low weight and only a limited effect on the index as a whole. Monetary policy has the potential to influence house prices. The central bank takes the housing market into account when setting monetary conditions affecting the entire economy, and applies targeted macroprudential tools where appropriate.

—

1 The motivation for, and construction of, this index was described in the box An experimental price index including prices of older properties in Inflation Report III/2017.

2 It now takes around 16 net annual disposable incomes per capita to purchase an average 60 m^2 apartment, as against just 13 in 2016.

3 See Housing Affordability in Cities in the Czech Republic, OECD (2021).

4 Czech households account for around 93% of new mortgage loans provided.

5 The box Household savings, net wealth and consumption in the Autumn 2023 MPR covered this topic in more detail.

6 The correlation coefficient between the volume of time deposits and the deposit interest rate is high (0.83).

7 See Šustek, R., Zapletalová, L. (2023): Snížila by větší bytová výstavba cenový růst nemovitostí v letech 2013–2021? Pravděpodobně ne (*Would real house prices have risen more slowly if more new housing had been built in 2013–2021? Probably not*), IDEA, Economics Institute of the Czech Academy of Sciences.

8 This is a reworked version of the model in Pfeifer, L., Pikhart, Z. (2015): Vliv měnových podmínek na jednotlivé kategorie cen v České republice v kontextu měnové a makroobezřetnostní politiky (*The effect of monetary conditions on individual categories of prices in the Czech Republic*), Politická ekonomie 8/2015.

9 Brůha, J., Tonner, J., Tvrz, S., Vašíček, O. (2024): Implications of real estate price development for monetary policy from the perspective of a DSGE model, CNB draft. This is an extension of the model in Tonner, J., Brůha, J. (2014): The Czech housing market through the lens of a DSGE model containing collateral-constrained households, CNB WP 9/2014.

Abbreviations

AEIS	Average Earnings Information System
BoE	Bank of England
BoJ	Bank of Japan
CF	Consensus Forecasts
CNB	Czech National Bank
CPI	consumer price index
CPIH	experimental consumer price index incorporating prices of older properties
CZK	Czech koruna
CZSO	Czech Statistical Office
DSTI	debt service-to-income
DTI	debt-to-income
ECB	European Central Bank
EEA	European Economic Area
EIA	US Energy Information Administration
EIA	Environmental Impact Assessment
EIU	Economist Intelligence Unit
ESA	European System of Accounts
ESCB	European System of Central Banks
ESI	Economic Sentiment Indicator
ESR	electronic sales registration
EU	European Union
EUR	euro
EURIBOR	Euro Interbank Offered Rate
FDI	foreign direct investment
FECF	Foreign Exchange Consensus Forecasts
Fed	US central bank
FMIE	Financial Market Inflation Expectations
FOMC	Federal Open Market Committee
FRA	forward rate agreement
GDP	gross domestic product
GNP	gross national product
GVA	gross value added
GVCs	global value chains
HP filter	Hodrick-Prescott filter
HPI	house price index
ICT	information and communications technology
IEA	International Energy Agency
Ifo	index of economic confidence in Germany
ILO	International Labour Organization
IMF	International Monetary Fund
IR	Inflation Report
IRI	Institute for Regional Information
IRS	interest rate swap
JPY	Japanese yen
LFS	Labour Force Survey
LIBOR	London Interbank Offered Rate
LTV	loan-to-value
LUCI	Labour Utilisation Composite Index
M1, M3	monetary aggregates
MFIs	monetary financial institutions
MLSA	Ministry of Labour and Social Affairs
m-o-m	month-on-month
MPR	Monetary Policy Report
NAIRU	non-accelerating inflation rate of unemployment
NBS	National Bank of Slovakia
OECD	Organisation for Economic Co-operation and Development
OPEC+	The OPEC member countries and another ten oil-exporting countries (the most important being Russia, Mexico and Kazakhstan)
PMI	Purchasing Managers Index
pp	percentage points
PPI	producer price index
PRIBOR	Prague Interbank Offered Rate
q-o-q	quarter-on-quarter
repo rate	repurchase agreement rate
rhs	right-hand scale
USD	US dollar
VAT	value added tax
WTI	West Texas Intermediate
y-o-y	year-on-year

Key macroeconomic indicators

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
DEMAND AND SUPPLY												
Gross domestic product												
GDP (CZK bn, current p., seas. adjusted)	4653.8	4841.1	5185.3	5481.3	5891.4	5830.0	6306.1	7048.5	7626.6	**8030.7**	**8442.0**	**8825.4**
GDP (%, y-o-y, real terms, seas. adjusted)	5.0	2.5	5.3	2.8	3.5	-5.3	4.0	2.9	0.0	**1.0**	**2.4**	**2.4**
GDP (%, q-o-q, real terms, seas. adjusted)	-	-	-	-	-	-	-	-	-	**-**	**-**	**-**
Household consumption (%, y-o-y, real terms, seas. adjusted)	3.7	3.5	4.5	3.4	3.0	-6.6	4.1	0.4	-2.9	**1.6**	**2.2**	**2.8**
Government consumption (%, y-o-y, real terms, seas. adjusted)	1.8	2.4	1.7	3.5	2.6	4.1	1.5	0.4	3.5	**3.4**	**1.3**	**0.8**
Gross capital formation (%, y-o-y, real terms, seas. adjusted)	11.7	-3.8	5.6	6.3	5.6	-9.3	18.4	10.2	-6.4	**-4.6**	**7.5**	**3.9**
Gross fixed capital formation (%, y-o-y, real terms, seas. adjusted)	8.9	-2.1	3.1	8.9	7.4	-4.8	6.7	6.3	2.7	**0.9**	**2.9**	**2.7**
Exports of goods and services (%, y-o-y, real terms, seas. adjusted)	6.1	3.9	7.5	3.5	1.2	-8.6	8.0	5.2	3.0	**1.1**	**3.2**	**4.6**
Imports of goods and services (%, y-o-y, real terms, seas. adjusted)	6.7	2.4	6.3	5.5	1.2	-8.5	13.6	6.0	-0.6	**-0.2**	**4.9**	**5.3**
Net exports (percentage points, contributions to GDP growth)	-0.1	1.4	1.4	-1.1	0.1	-0.6	-2.8	-0.3	2.7	**0.9**	**-0.8**	**-0.1**
PRICES												
Main price indicators												
Consumer Price Index (%, y-o-y, average)	0.3	0.7	2.5	2.1	2.8	3.2	3.8	15.1	10.7	**2.5**	**2.6**	**2.2**
Administered prices (%, y-o-y, average, 15.01%*)	0.0	0.2	0.0	1.8	4.4	3.1	-0.2	20.9	27.8	**6.2**	**1.6**	**2.0**
Food prices (incl. alcoholic beverages and tobacco, %, y-o-y, average, 26.21%*)	0.1	0.2	3.7	1.6	2.6	4.2	2.1	12.9	10.0	**0.9**	**3.8**	**2.2**
Core inflation (%, y-o-y, average, 55.27%*)	1.2	1.2	2.4	2.1	2.7	3.3	4.8	13.2	7.6	**2.5**	**2.5**	**2.2**
Fuel prices (%, y-o-y, average, 3.51%*)	-13.5	-8.5	6.7	6.3	-0.4	-11.4	16.7	33.6	-12.1	**-0.7**	**-3.9**	**-0.2**
Monetary policy-relevant inflation (%, y-o-y, average)	0.2	0.5	2.5	2.1	2.9	3.2	3.9	14.6	10.6	**2.4**	**2.5**	**2.1**
Partial price indicators												
Industrial producer prices (%, y-o-y, average)	-3.2	-3.3	1.8	2.0	2.6	0.1	7.1	24.3	5.0	**0.7**	**1.1**	**1.3**
Agricultural prices (%, y-o-y, average)	-5.9	-5.8	7.4	-0.1	5.4	-3.8	7.4	31.8	-5.5	**-7.9**	**-0.9**	**-1.7**
GDP deflator (%, y-o-y, seas. adjusted)	1.2	1.5	1.7	2.8	3.8	4.5	4.0	8.7	8.2	**4.2**	**2.6**	**2.0**
LABOUR MARKET												
Average monthly wage (%, y-o-y, nominal terms)	3.2	4.4	6.7	8.2	7.9	4.6	5.8	4.3	8.0	**6.4**	**5.7**	**5.1**
Average monthly wage in market sectors (%, y-o-y, nominal terms)	3.2	4.3	6.7	7.7	7.6	4.1	6.1	4.7	8.4	**7.2**	**5.7**	**5.2**
Average monthly wage in non-market sectors (%, y-o-y, nominal terms)	3.3	4.8	7.1	10.2	9.2	6.9	4.4	2.6	6.0	**2.7**	**6.1**	**4.3**
Average monthly wage (%, y-o-y, real terms)	2.8	3.7	4.1	5.9	4.9	1.4	2.0	-9.3	-2.4	**3.8**	**3.0**	**2.8**
Unit labour costs (%, y-o-y)	0.1	3.0	3.8	6.5	4.2	5.9	3.1	6.1	7.8	**4.7**	**3.3**	**2.8**
Aggregate labour productivity (%, y-o-y)	3.5	1.5	3.8	1.7	3.7	-3.0	3.0	1.8	-1.1	**0.6**	**1.9**	**2.0**
ILO general unemployment rate (%, average, age 15–64, seas. adjusted)	5.1	4.0	2.9	2.2	2.0	2.6	2.8	2.2	2.6	**2.7**	**2.9**	**3.0**
Share of unemployed persons (MLSA, %, average, seas. adjusted)	6.5	5.5	4.2	3.2	2.8	3.6	3.8	3.4	3.6	**3.8**	**4.0**	**4.0**
Employment (ILO, %, y-o-y)	1.3	1.8	1.5	-1.4	0.1	-1.4	0.3	-1.6	1.5	**2.7**	**0.2**	**0.4**
Full-time employment (%, y-o-y)	2.1	1.8	2.2	1.5	-0.3	-1.7	0.2	0.7	-0.1	**0.2**	**0.2**	**0.2**
PUBLIC FINANCE												
Government budget balance (ESA2010, CZK bn, current prices)	-31.0	33.2	75.6	48.3	16.7	-329.3	-312.3	-216.3	-288.1	**-213.2**	**-195.5**	**-193.7**
Government budget balance/GDP** (%, nominal terms)	-0.7	0.7	1.5	0.9	0.3	-5.6	-5.0	-3.1	-3.8	**-2.7**	**-2.3**	**-2.2**
Structural balance/GDP (%, nominal terms)	-0.9	0.1	0.8	0.4	-0.5	-5.8	-5.3	-3.2	-3.4	**-2.3**	**-2.3**	**-2.1**
Government debt (ESA2010, CZK bn, current prices)	1836.0	1754.7	1749.7	1734.6	1740.3	2149.7	2566.8	2997.6	3234.0	**3485.4**	**3713.2**	**3937.8**
Government debt/GDP** (%, nominal terms)	39.5	36.2	33.8	31.7	29.6	36.9	40.7	42.5	42.4	**43.5**	**44.0**	**44.7**
EXTERNAL RELATIONS												
Current account												
Goods and services, net (CZK bn, current prices)	274.3	365.1	394.2	332.6	358.4	388.8	232.2	75.9	383.8	**522.3**	**419.5**	**433.6**
Current account (CZK bn, current prices)	20.7	85.2	79.8	21.5	19.6	102.5	-129.7	-330.3	23.7	**124.9**	**19.5**	**24.3**
Current account/GDP (%, nominal terms)	0.4	1.8	1.5	0.4	0.3	1.8	-2.1	-4.7	0.3	**1.6**	**0.2**	**0.3**
Foreign direct investment												
Direct investment (CZK bn, current prices)	49.7	-186.5	-45.9	-51.0	-137.1	-149.1	-28.5	-83.5	-16.3	**-5.0**	**-30.0**	**-20.0**
Exchange rates												
CZK/USD (average)	24.6	24.4	23.4	21.7	22.9	23.2	21.7	23.4	22.2	**23.1**	**22.9**	**22.7**
CZK/EUR (average)	27.3	27.0	26.3	25.6	25.7	26.5	25.6	24.6	24.0	**25.1**	**25.4**	**25.5**
MONEY AND INTEREST RATES												
M3 (%, y-o-y, average)	7.3	9.1	11.7	6.6	6.3	9.0	9.6	6.4	9.0	**6.1**	**8.2**	**7.9**
2W repo rate (%, average)	0.1	0.1	0.2	1.1	1.9	0.8	0.9	5.9	7.0	**5.1**	**3.1**	**2.9**
3M PRIBOR (%, average)	0.3	0.3	0.4	1.3	2.1	0.9	1.1	6.3	7.1	**4.9**	**3.2**	**3.0**
EXTERNAL ASSUMPTIONS												
Foreign GDP (%, y-o-y, seas. adjusted, effective EA)	2.0	2.0	2.8	1.7	1.4	-5.4	4.6	2.3	0.4	**0.5**	**0.9**	**1.5**
Foreign GDP (%, q-o-q, seas. adjusted, effective EA)	-	-	-	-	-	-	-	-	-	**-**	**-**	**-**
Foreign HICP (%, y-o-y, seas. adjusted, effective EA)	0.4	0.2	1.6	2.0	1.5	0.6	2.9	8.9	6.7	**2.5**	**2.1**	**2.1**
Foreign PPI (%, y-o-y, seas. adjusted, effective EA)	-2.3	-2.2	2.4	3.1	1.1	-1.3	9.6	32.8	2.8	**-5.5**	**1.1**	**0.6**
Brent crude oil (in USD/barrel, average)	53.6	45.0	54.8	71.5	64.2	43.2	70.8	98.9	82.2	**80.6**	**75.0**	**73.2**
3M EURIBOR (%, average)	0.0	-0.3	-0.3	-0.3	-0.4	-0.4	-0.5	0.3	3.4	**3.6**	**2.7**	**2.5**
USD/EUR (average)	1.11	1.11	1.13	1.18	1.12	1.14	1.18	1.05	1.08	**1.09**	**1.11**	**1.12**

* constant weights in current consumer basket
** CNB calculation
- data not available/forecasted/released
data in bold = CNB forecast

	2024				2025				2026			
	QI	QII	QIII	QIV	QI	QII	QIII	QIV	QI	QII	QIII	QIV
DEMAND AND SUPPLY												
Gross domestic product												
GDP (CZK bn, current p., seas. adjusted)	1964.9	1999.8	**2021.1**	**2044.9**	**2073.2**	**2098.1**	**2123.7**	**2147.0**	**2171.0**	**2194.1**	**2218.1**	**2242.3**
GDP (%, y-o-y, real terms, seas. adjusted)	0.4	0.6	**1.3**	**1.7**	**2.1**	**2.4**	**2.7**	**2.6**	**2.5**	**2.5**	**2.4**	**2.4**
GDP (%, q-o-q, real terms, seas. adjusted)	0.4	0.4	**0.3**	**0.7**	**0.7**	**0.7**	**0.6**	**0.6**	**0.6**	**0.6**	**0.6**	**0.6**
Household consumption (%, y-o-y, real terms, seas. adjusted)	1.7	1.0	**1.9**	**1.7**	**1.6**	**2.1**	**2.5**	**2.7**	**2.9**	**2.9**	**2.8**	**2.8**
Government consumption (%, y-o-y, real terms, seas. adjusted)	3.2	4.4	**2.9**	**2.9**	**2.2**	**0.7**	**1.3**	**0.9**	**0.9**	**0.9**	**0.8**	**0.7**
Gross capital formation (%, y-o-y, real terms, seas. adjusted)	-9.9	-7.1	**-4.9**	**4.1**	**6.3**	**8.5**	**8.4**	**6.8**	**5.2**	**4.1**	**3.4**	**3.1**
Gross fixed capital formation (%, y-o-y, real terms, seas. adjusted)	-0.1	0.7	**1.1**	**1.8**	**3.7**	**2.3**	**2.9**	**2.7**	**2.7**	**2.9**	**2.6**	**2.6**
Exports of goods and services (%, y-o-y, real terms, seas. adjusted)	-0.1	0.4	**2.3**	**1.8**	**2.5**	**2.8**	**3.5**	**4.0**	**4.4**	**4.6**	**4.7**	**4.8**
Imports of goods and services (%, y-o-y, real terms, seas. adjusted)	-2.9	-1.5	**0.5**	**3.0**	**4.0**	**4.7**	**5.3**	**5.5**	**5.5**	**5.3**	**5.2**	**5.1**
Net exports (percentage points, contributions to GDP growth)	1.9	1.3	**1.2**	**-0.6**	**-0.7**	**-0.9**	**-0.9**	**-0.7**	**-0.4**	**-0.2**	**0.0**	**0.1**
PRICES												
Main price indicators												
Consumer Price Index (%, y-o-y, average)	2.1	2.5	2.3	**3.0**	**2.9**	**2.6**	**2.6**	**2.4**	**2.2**	**2.3**	**2.2**	**2.1**
Administered prices (%, y-o-y, average, 15.01%*)	6.2	5.9	5.8	**6.8**	**1.8**	**1.3**	**1.5**	**1.9**	**1.9**	**2.0**	**2.0**	**2.0**
Food prices (incl. alcoholic beverages and tobacco, %, y-o-y, average, 26.21%*)	-1.1	0.1	1.2	**3.4**	**4.7**	**4.1**	**3.5**	**2.8**	**2.3**	**2.3**	**2.1**	**2.1**
Core inflation (%, y-o-y, average, 55.27%*)	2.8	2.4	2.3	**2.4**	**2.5**	**2.5**	**2.5**	**2.3**	**2.2**	**2.2**	**2.2**	**2.1**
Fuel prices (%, y-o-y, average, 3.51%*)	0.4	7.4	-3.6	**-7.2**	**-5.3**	**-6.8**	**-2.7**	**-0.6**	**-0.8**	**0.6**	**-0.9**	**0.4**
Monetary policy-relevant inflation (%, y-o-y, average)	2.1	2.4	2.2	**2.9**	**2.7**	**2.4**	**2.5**	**2.3**	**2.1**	**2.1**	**2.1**	**2.0**
Partial price indicators												
Industrial producer prices (%, y-o-y, average)	-0.9	1.1	1.2	**1.5**	**0.2**	**1.0**	**1.6**	**1.7**	**1.3**	**1.3**	**1.3**	**1.2**
Agricultural prices (%, y-o-y, average)	-17.3	-10.4	-1.5	**-0.2**	**-0.4**	**0.2**	**-1.0**	**-2.6**	**-2.4**	**-1.8**	**-1.5**	**-1.3**
GDP deflator (%, y-o-y, seas. adjusted)	4.1	4.1	**4.3**	**4.4**	**3.4**	**2.5**	**2.3**	**2.3**	**2.2**	**2.1**	**2.0**	**2.0**
LABOUR MARKET												
Average monthly wage (%, y-o-y, nominal terms)	7.2	6.5	**6.1**	**5.8**	**5.4**	**5.6**	**6.1**	**6.0**	**5.3**	**5.1**	**5.0**	**4.8**
Average monthly wage in market sectors (%, y-o-y, nominal terms)	8.3	7.3	**6.8**	**6.4**	**5.2**	**5.5**	**6.0**	**5.9**	**5.6**	**5.3**	**5.1**	**4.9**
Average monthly wage in non-market sectors (%, y-o-y, nominal terms)	2.5	2.8	**2.5**	**2.9**	**6.1**	**5.9**	**6.2**	**6.2**	**3.9**	**4.1**	**4.4**	**4.4**
Average monthly wage (%, y-o-y, real terms)	5.0	4.0	**3.6**	**2.7**	**2.4**	**2.9**	**3.3**	**3.4**	**3.0**	**2.8**	**2.7**	**2.6**
Unit labour costs (%, y-o-y)	6.5	4.8	**4.3**	**3.4**	**3.0**	**3.3**	**3.4**	**3.5**	**2.9**	**2.8**	**2.8**	**2.6**
Aggregate labour productivity (%, y-o-y)	-0.3	0.7	**0.7**	**1.1**	**1.2**	**1.9**	**2.3**	**2.2**	**2.0**	**2.0**	**2.0**	**2.0**
ILO general unemployment rate (%, average, age 15–64, seas. adjusted)	2.7	2.6	**2.7**	**2.7**	**2.8**	**2.8**	**2.9**	**2.9**	**3.0**	**3.0**	**3.0**	**3.0**
Share of unemployed persons (MLSA, %, average, seas. adjusted)	3.7	3.8	**3.9**	**3.9**	**3.9**	**3.9**	**4.0**	**4.0**	**4.0**	**4.0**	**4.0**	**4.0**
Employment (ILO, %, y-o-y)	3.8	2.0	**2.5**	**2.5**	**-0.4**	**0.4**	**0.4**	**0.4**	**0.4**	**0.4**	**0.4**	**0.4**
Full-time employment (%, y-o-y)	0.0	0.0	**0.2**	**0.3**	**0.2**	**0.2**	**0.2**	**0.2**	**0.2**	**0.2**	**0.2**	**0.2**
PUBLIC FINANCE												
Government budget balance (ESA2010, CZK bn, current prices)	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Government budget balance/GDP** (%, nominal terms)	-	-	-	-	-	-	-	-	-	-	-	-
Structural balance/GDP (%, nominal terms)	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Government debt (ESA2010, CZK bn, current prices)	-	-	-	-	-	-	-	-	-	-	-	-
Government debt/GDP** (%, nominal terms)	-	-	-	-	-	-	-	-	-	-	-	-
EXTERNAL RELATIONS												
Current account												
Goods and services, net (CZK bn, current prices)	160.5	152.0	**116.5**	**93.2**	**143.0**	**124.2**	**77.8**	**74.6**	**131.7**	**128.0**	**88.3**	**85.6**
Current account (CZK bn, current prices)	100.2	-1.7	**27.0**	**-0.7**	**92.4**	**-3.5**	**-51.9**	**-17.5**	**77.5**	**-2.0**	**-42.9**	**-8.3**
Current account/GDP (%, nominal terms)	5.4	-0.1	**1.3**	**0.0**	**4.7**	**-0.2**	**-2.4**	**-0.8**	**3.8**	**-0.1**	**-1.9**	**-0.4**
Foreign direct investment												
Direct investment (CZK bn, current prices)	-37.9	24.5	**4.2**	**4.2**	**-7.5**	**-7.5**	**-7.5**	**-7.5**	**-5.0**	**-5.0**	**-5.0**	**-5.0**
Exchange rates												
CZK/USD (average)	23.1	23.2	22.9	**23.0**	**23.0**	**23.0**	**22.9**	**22.9**	**22.8**	**22.8**	**22.7**	**22.5**
CZK/EUR (average)	25.1	25.0	25.2	**25.3**	**25.4**	**25.4**	**25.5**	**25.5**	**25.5**	**25.6**	**25.6**	**25.4**
MONEY AND INTEREST RATES												
M3 (%, y-o-y, average)	7.9	5.7	5.7	**5.1**	**6.4**	**7.8**	**8.8**	**9.6**	**8.8**	**8.1**	**7.5**	**7.3**
2W repo rate (%, average)	6.4	5.4	4.6	**4.0**	**3.5**	**3.1**	**3.0**	**3.0**	**2.9**	**2.9**	**2.9**	**2.9**
3M PRIBOR (%, average)	6.2	5.2	4.4	**3.9**	**3.4**	**3.1**	**3.1**	**3.1**	**3.0**	**3.0**	**3.0**	**3.0**
EXTERNAL ASSUMPTIONS												
Foreign GDP (%, y-o-y, seas. adjusted, effective EA)	0.5	0.5	**0.4**	**0.7**	**0.6**	**0.8**	**1.0**	**1.2**	**1.3**	**1.4**	**1.5**	**1.6**
Foreign GDP (%, q-o-q, seas. adjusted, effective EA)	0.3	0.0	**0.1**	**0.2**	**0.2**	**0.3**	**0.3**	**0.4**	**0.4**	**0.4**	**0.4**	**0.4**
Foreign HICP (%, y-o-y, seas. adjusted, effective EA)	2.9	2.5	**2.2**	**2.4**	**2.1**	**2.0**	**2.1**	**2.1**	**2.1**	**2.1**	**2.1**	**2.1**
Foreign PPI (%, y-o-y, seas. adjusted, effective EA)	-7.8	-6.1	**-4.4**	**-3.6**	**0.9**	**1.9**	**0.9**	**0.7**	**0.5**	**0.5**	**0.7**	**0.8**
Brent crude oil (in USD/barrel, average)	81.8	85.0	78.7	**76.9**	**75.9**	**75.3**	**74.7**	**74.1**	**73.7**	**73.3**	**73.1**	**72.8**
3M EURIBOR (%, average)	3.9	3.8	3.6	**2.9**	**2.8**	**2.7**	**2.6**	**2.6**	**2.6**	**2.5**	**2.5**	**2.5**
USD/EUR (average)	1.09	1.08	1.10	**1.10**	**1.10**	**1.11**	**1.11**	**1.11**	**1.12**	**1.12**	**1.12**	**1.13**

* constant weights in current consumer basket
** CNB calculation
\- data not available/forecasted/released
data in bold = CNB forecast

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