Czech Republic

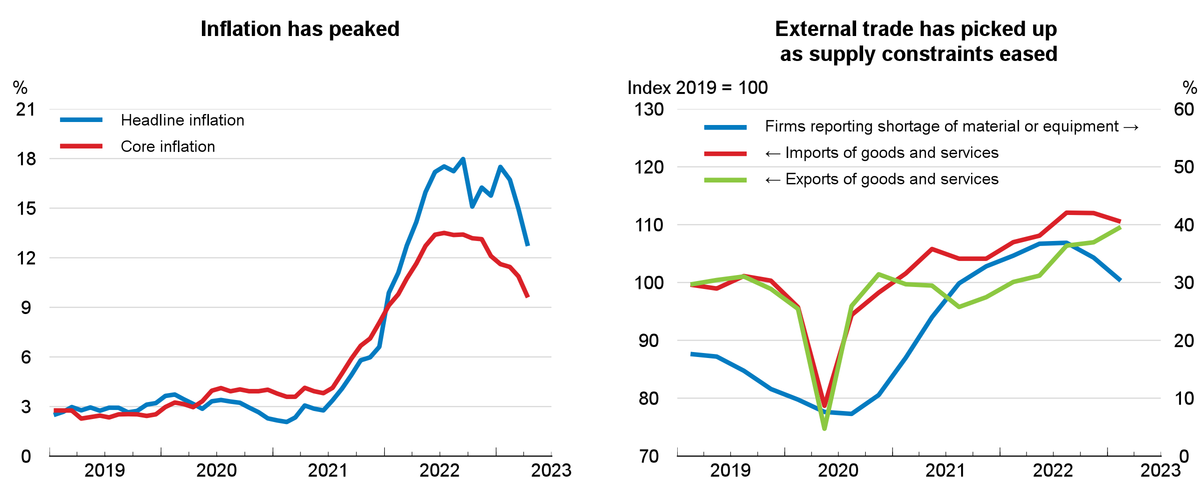
GDP growth will slow to 0.3% in 2023, before picking up to 2.4% in 2024. In 2023, high energy prices, tight financing conditions and weak sentiment will hold back private investment, and still elevated inflation will constrain private consumption. Private consumption will pick up in 2024, underpinned by growing real wages. Inflation will start falling from currently high levels but will only approach the 2% target towards the end of 2024. The unemployment rate will remain low, close to 3%.

Macroeconomic policy needs to maintain a tight stance until inflation expectations are firmly under control, while monitoring risks to financial stability. Fiscal consolidation should be pursued to rebuild fiscal buffers. Measures to counter high energy prices should become increasingly targeted at those who are not sufficiently protected by the general social protection system, while preserving incentives for energy savings. Unleashing labour supply and accelerating the green transition would support sustainable growth.

The economy has gone through a mild recession

GDP stagnated (0% quarterly growth) in the first quarter of 2023. This followed a shallow recession in the second half of 2022, on the back of high energy prices, tighter financing conditions, and continued high uncertainty. Consumer price inflation has risen to levels not seen in almost 30 years and stood at 12.7% in April 2023. Economic sentiment dropped sharply, dampening household consumption and private investment. Elevated inflation squeezed real household incomes. However, inflation pressures have started abating and core inflation dropped from high levels. Exports rebounded, as supply bottlenecks started easing. Consumer sentiment started to recover. The labour market remains tight and the unemployment rate very low, at 2.7% in the first quarter of 2023.

Czech Republic



Source: Czech Statistical Office; and Czech National Bank.

StatLink https://stat.link/o5tulv

Czech Republic: Demand, output and prices

Czech Republic	2019	2020	2021	2022	2023	2024
	Current prices CZK billion	Percentage changes, volume (2015 prices)				
GDP at market prices	5 793.9	-5.5	3.5	2.5	0.3	2.4
Private consumption	2 712.0	-7.2	4.1	-0.9	-2.7	2.4
Government consumption	1 134.5	4.2	1.4	0.6	3.0	1.2
Gross fixed capital formation	1 568.2	-6.0	0.8	6.2	1.3	0.9
Final domestic demand	5 414.7	-4.5	2.5	1.4	-0.3	1.7
Stockbuilding[1]	29.8	-0.9	4.8	0.9	-0.7	0.0
Total domestic demand	5 444.5	-5.4	7.6	2.3	-1.0	1.6
Exports of goods and services	4 284.6	-8.1	6.8	5.7	4.4	4.1
Imports of goods and services	3 935.2	-8.2	13.2	5.7	2.9	3.0
Net exports[1]	349.4	-0.4	-3.6	0.2	1.1	0.8
Memorandum items						
GDP deflator	_	4.3	3.3	8.6	9.3	3.7
Consumer price index	_	3.2	3.8	15.1	12.2	3.4
Core inflation index[2]	_	3.6	5.0	12.2	9.0	4.1
Unemployment rate (% of labour force)	_	2.5	2.8	2.3	2.8	3.0
Household saving ratio, net (% of disposable income)	_	14.7	14.8	12.5	12.2	11.9
General government financial balance (% of GDP)	_	-5.8	-5.1	-3.6	-3.8	-2.7
General government gross debt (% of GDP)	_	47.0	48.5	48.1	50.8	52.6
General government debt, Maastricht definition[3] (% of GDP)	_	37.6	42.0	44.1	46.8	48.7
Current account balance (% of GDP)	_	2.0	-2.8	-6.1	-2.9	-3.4

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 113 database.

StatLink https://stat.link/ixo6lw

Prior to Russia's war of aggression against Ukraine, Russia accounted for more than half of crude oil imports and virtually all gas consumption. In 2022, gas consumption was roughly 20% lower than in 2021 and total domestic gas reserves at end-2022 were high. The projections assume no major supply issues next winter. The government has introduced measures to cushion the impact of high energy prices, including support to households and companies and price caps on energy, partly financed by a newly introduced tax on the excess profits of energy producers, traders and banks. The Czech Republic has welcomed a large number of Ukrainian refugees. By early May, around 330 000 refugees were registered for Temporary Protection. About 40% of refugees of working age were employed as of late April 2023.

Macroeconomic policy has been tightened

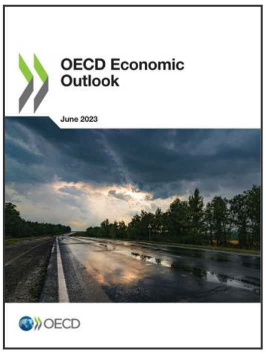
The Czech National Bank (CNB) has tightened monetary policy significantly to counter rapid increases in core inflation and rising inflation expectations. Between June 2021 and June 2022, the CNB raised the policy interest rate from 0.25% to 7%, after which it paused its tightening cycle. Property and mortgage markets have started to slow significantly. A gradual easing cycle is projected to start in the first quarter of 2024. In hindsight, macroeconomic policy provided too much stimulus in 2020 and 2021. Fiscal policy has introduced too many untargeted measures. The fiscal situation has deteriorated and the fiscal rules have been loosened. Recently introduced measures to cushion the impact of high energy prices are assumed to stay in place until the end of 2023, contingent on the evolution of market prices. In May 2023, the government announced a package of spending and revenue measures to undertake structural fiscal consolidation of 1.2 percentage points of GDP in 2023 and a further 0.6 percentage points in 2024. The consolidation package has yet to be adopted by parliament and is not incorporated in the projections.

GDP growth will remain subdued in 2023, before picking up in 2024

Private consumption will remain weak in 2023 due to elevated inflation and falling real incomes. Private investment will pick up only gradually due to tighter financing conditions. On the other hand, public investment will grow rapidly in 2023, due to the end of the EU 2014-2020 programming period. In 2024, stronger growth in trading partners will support exports and trade. Inflation will slowly approach the 2% target and real wage growth will turn positive, boosting private consumption. The unemployment rate will remain close to 3%. The outlook is uncertain. Energy supply disruptions could restrict economic activity. Unexpected further rises in commodity and energy prices, a steep depreciation of the koruna or derailed inflation expectations could make high inflation more persistent and delay monetary easing. Spillovers from banking crises abroad or a sharp correction in housing prices could threaten financial stability.

Unleashing labour supply and accelerating the green transition would support growth

Interest rates will have to remain elevated until inflationary pressures are well controlled. The authorities need to continue closely monitoring risks in the housing market. Fiscal policy should avoid stimulating aggregate demand in order not to undermine monetary policy. Fiscal support measures to cushion elevated energy prices should be well-targeted and maintain incentives for energy savings. Incentives to boost energy efficiency, including for heating and insulation in housing, should be strengthened to reduce reliance on coal and help households cope with high energy prices. Stepping up investment in renewable energy would make the recovery more sustainable. Boosting labour supply of mothers, by boosting the supply of childcare and shortening the maximum length of parental leave, and also older workers, together with improvements to skills provision and redesigning immigration policy, would help attract and retain skilled labour.



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