**CBA'S MACROECONOMIC FORECAST**

**November 2011: this year, Czech economy will grow at a slower pace than expected, only by 2.6%. It will accelerate to 3.9% next year, but inflation will be the highest since 2008.**

**Prague, November 11, 2021 - The chief economists of the banks represented in the prognostic panel of the Czech Banking Association (the CBA) have revised their estimate of the domestic economy's growth downward for both this year and next. Given the continuing problems in subcontracting chains and to rising inflation, the domestic economy can be expected to grow by 2.6% this year, as compared with the August estimate of 3.4%. The estimate for 2022 has also been revised downward, from 4.5% to 3.9%. Inflation is expected to exceed 5% next year and will be the highest since 2008. However, the appreciable uncertainty of the forecast is also caused by a potential response to the current extraordinary increase of energy prices taken by the government. This should not, however, change the trajectory of the Czech National Bank's interest rate increase in the coming months. The koruna should nevertheless strengthen only slightly next year.**

**The pandemic situation continues to disrupt production and to limit the recovery of global economy**

Economic indicators in recent months have indicated that the post-pandemic recovery is facing a number of issues that are retreating more slowly than has been expected even in the middle of the year. Disrupted supply chains remain a serious complication, making it difficult to supply the necessary parts and causing their prices to increase rapidly. The issue is the divergent way in which the pandemic situation develops within the global economy. Many countries thus struggled with the pandemic even during the summer, which disrupted their production capacities, while in certain economies, demand grew in the hope that the pandemic would end due to the vaccination. The mismatch between supply and demand thus produces a number of adverse effects, including a shortage of goods and their rising prices. In the second half of this year, a number of economies were hit by the energy crisis, which brought about a multiple increase in energy prices, faced by a large part of the world economy. In Europe, the situation has reached a highly extreme level due to the concurrence of a number of adverse effects. This factor will also disrupt the recovery of the European economies not only this year, but also in 2022.

**Jakub Seidler, Chief Economist of the Czech banking Association:**

*"The recovery of the world economy in the second half of this year was still significantly affected by disrupted supply chains and by lack of materials. Although these problems are slightly retreating, they will probably persist in the first half of next year as well. Add to that the energy crisis and surging energy costs will negatively affect both enterprises and household consumption.”*

**Growth of the domestic economy is weaker than had been expected before the holiday months**

**According to the new CBA forecast, the growth of the domestic economy will reach 2.6% this year, while the August forecast expected it to growth at 3.4%.** The pace of recovery of the domestic economy in the second half of this year will thus be significantly below the assumptions of the previous forecast. Not only was the economic growth in the third quarter slightly disappointing, but overly optimistic values cannot be expected even at the end of this year ​​due to the persisting problems in supply chains and to accelerating inflation. While the August forecast estimated growth of at least one percent in the last quarter of this year, the consensus now sees quarter-on-quarter stagnation in the last quarter, and some estimates even suggest a slight economic downturn. The suspension of production by car manufacturers during October will have a negative effect that will be reflected in the last quarter.

**Next year, the CBA prognostic panel expects economy to grow by 3.9%.** Compared to the previous forecast, which expected growth of 4.5%, this is a weaker value, mainly due to a faster inflation affecting household consumption and also to the ongoing issues in supply chains. Although they are gradually improving, they will probably at least partially persist during the first half of next year. However, investment activity should become an engine for growth, which should accelerate significantly compared to this year. There are large differences between forecasts as regards household consumption (growth between 2.4% up to 6.5%). Some estimates suggest a more pronounced slowdown in household consumption due to the impact of higher inflation and a general increase in household debt, which, combined with higher interest rates, will deprive many households of a part of their income spent on consumption. Conversely, other estimates suggest a certain dissolution of accumulated savings and a return of consumption to the pre-pandemic levels.

**Wages will rise, but they will not compensate for the rise in inflation next year**

Although the labor market has ceased to be a major barrier to growth in recent surveys performed among businesses and it has been overcome by a shortage of materials, this does not mean that the availability of workforce has improved - the shortage of materials has only become a more acute issue. **The** l**abor market in the domestic economy thus still remains overheated and complicates the further development of many businesses**. At the same time, as in the past, estimates of the development of unemployment are starting to provide a positive surprise and they are again moving towards lower values. From this year's 3.8%, the share of unemployed people should fall to 3.4% next year. This is only a slightly higher value than in 2018 (3.2% according to the Ministry of Labor and Social Affairs). Although problems in industry may cause redundancies in some businesses, the mismatch between job vacancies and the number of unemployed is so significant that the CBA panel does not anticipate a visible impact on the unemployment rate.

**Jaromír Šindel, the Chief Economist of Citibank:**

*"Despite the pandemic, the labor market has restored its inflationary pressures relatively quickly. This is also due to the relatively high share of foreign workers and the demand for them will increase among our regional neighbors as their demographic situation will deteriorate faster than in our case. In addition, the problems in the car industry do not seem to have a negative impact on the demand for workforce in other sectors."*

Given the above-mentioned developments in the labor market, it is expected that the increase of wages and salaries will ultimately be faster this year, not least due to the special incentives in the healthcare sector. **Wages and salaries are expected to increase by 5.8% this year. Growth will continue next year, partly supported by a 6.6% increase in the minimum wage and the associated guaranteed wages.** The expected lower wage growth in the public sector will have the opposite effect. Thus, the combination of a faster inflation and persisting economic uncertainties this year, limiting the bargaining power of employees, is likely to lead to a slight decline in real wages next year, which is likely to be accompanied by a decline in savings.

**Inflation to accelerate; it may reach the 2008 levels**

**The acceleration of inflation has been above expectations in the second half of this year and it has led to significant revisions to inflation estimates for this year and next**. This acceleration will be associated in particular with housing prices, with a more significant rise in energy prices expected at the end of the year, which has not affected domestic inflation so much up to now. Inflation is thus estimated to be around 6% at the end of this year and its possible further acceleration will be dampened by the planned reduction in VAT on energy. For the whole of this year, inflation will average 3.8%. **Inflation estimates for the next year are subject to considerable uncertainty, as it is not clear whether the reduction in VAT on energy will continue and at which reduced rate**. In this respect, the assumptions of the individual forecasts in the panel differ. Although **the median inflation rate for next year is 5.1%, some estimates are closer to 6%, and in general, the prevailing view among the prognostic panel experts was that inflation has the potential to surprise with higher values in the first half of the year.** The increase in prices will be relatively broad-based as a result of the impact brought by high energy prices. According to the current estimates, inflation should reach its peak in the first quarter of next year. However, most forecasts do not expect it to return below the 3% limit of the CNB's upper tolerance band before the end of next year.

**CNB rates to rise further; despite this, no significant appreciation of the crown is expected next year**

**Faster-than-expected price growth was reflected in significantly faster interest rate increases by the Czech National Bank. This year, the Czech National Bank undertook to increase its rates at an unprecedented pace and it has increased its base interest rate from 0.25% to 2.75% in a few months. However, in accordance with the CBA forecast, it has not yet said the last word this year. At the end of this year, the base rate should stand at approximately 3,25 %.** According to the CBA panel, however, next year's rate hikes will already be much more moderate and the median estimate assumes that rates at the end of the year should move between 3.25% and 3.5%. In addition, some panel members expect the CNB to start cutting rates again in the second half of next year, in anticipation of the slowing down of inflation beyond the 2022 horizon.

**Despite the increase of interest rates, the CBA's prognostic panel does not foresee a significant appreciation of the koruna**. It will average CZK 24.9 per euro next year, but it will not fall much below CZK 25 per euro by the end of the year either. In this respect, the CBA panel's estimates differ significantly from the CNB's latest forecast, which suggests that the koruna will appreciate to CZK 24 per euro by the end of next year.

**Higher inflation will lower the debt-to-GDP ratio**

The CBA forecast estimates the state deficit for this year at 7% of GDP, compared to 7.3% expected in August. Next year, the deficit should fall to 4.7%, leaving the outlook for 2022 unchanged from the August forecast. In general, the CBA panel economists assumed a somewhat higher level of consolidation than the pre-election rhetoric suggested for any government emerging from this year's parliamentary elections to the Chamber of Deputies. However, the higher growth in inflation, and hence nominal GDP, is obvious in the revision of the overall government debt/GDP ratio, which is expected to reach 43.6% next year, whereas the August forecast, expected debt to exceed 45% of GDP even with a higher economic growth.

**Petr Gapko, the Chief Economist of MONETA Money Bank:**

*"State debt is currently one of the most pressing economic problems. Inflation is likely to partially help ease the debt burden next year, but the government has to work significantly harder in the years ahead."*

**Corporate lending should accelerate next year**

The growth dynamics of mortgage loans have been entirely above standard this year, which is reflected in the double-digit year-on-year growth in the volume of mortgage loans. Next year, however, the CBA prognostic panel expects the growth rate of loans to households to slow down and reach 6% on average. By contrast, corporate loans should see faster credit growth next year, not only due to renewed investment activity but also to the need for operational financing. Thus, while the year-on-year growth rate of corporate loans is likely to fall slightly this year, it should grow by 4% on average next year. Compared to the previous forecast, the expected growth is weaker, which is also connected with higher interest rates that will dampen demand for credit.

**CBA's macroeconomic forecast in figures**

|  |  |  |  |
| --- | --- | --- | --- |
| **Indicator** | **2020**  **(Reality)** | **2021**  **(Forecast)** | **2022**  **(Forecast)** |
| **Real GDP (% yoy)** | -5.8 | **2.6** | **3.9** |
| **Share of unemployed people (MinLab, %, average)** | 3.6 | **3.8** | **3.4** |
| **Average nominal wage (% yoy)** | 3.1 | **5.8** | **4.9** |
| **Headline CPI (%, average)** | 3.2 | **3.8** | **5.1** |
| **Government deficit / surplus (% of GDP)** | -5.6 | **-7.0** | **-4.7** |
| **Government debt (% of GDP)** | 37.7 | **42.4** | **43.6** |
| **Household consumption (% yoy)** | -7.1 | **3.0** | **4.4** |
| **Government consumption (% yoy)** | 3.4 | **2.4** | **1.0** |
| **Fixed Investment (% yoy)** | -7.2 | **2.4** | **6.3** |
| **Exports (% yoy)** | -7.0 | **8.4** | **6.5** |
| **Imports (% yoy)** | -6.9 | **11.8** | **6.8** |
| **Real GDP growth in the euro area (% yoy)** | -6.9 | **5.0** | **4.0** |
| **CZK/EUR exchange rate (average)** | 26.5 | **25.6** | **24.9** |
| **CZK/EUR exchange rate (end of period)** | 26.2 | **25.2** | **24.8** |
| **Price of oil (USD per barrel): BRENT average** | 43.0 | **71.1** | **73.5** |
| **CNB 2T REPO rate (%, end of period)** | 0.25 | **3.25** | **3.38** |
| **ECB main rate (%, end of period)** | 0.0 | **0.0** | **0.0** |
| **3M-PRIBOR (%, average)** | 0.86 | **1.14** | **3.40** |
| **Bank loans to clients (% yoy, average)** | 4.9 | **4.9** | **5.1** |
| **Bank loans to households (% yoy, average)** | 6.5 | **7.7** | **6.5** |
| **Bank loans to (non-financial) corporations (% yoy, average)** | 3.2 | **-0.1** | **4.3** |
| **Customer bank deposits (% yoy, average)** | 10.8 | **8.8** | **6.0** |

**About the CBA forecast**

This forecast is based on contributions from analysts of 8 CBA member banks: Jan Vejmělek (Chief Economist at Komerční banka), Jaromír Šindel (Chief Economist at Citibank), Helena Horská (Chief Economist at Raiffeisenbank), Michal Skořepa (Macroeconomic Analyst at Česká spořitelna), Petr Dufek (Economic Analyst at ČSOB), Petr Gapko (Chief Economist at MONETA Money Bank) and Petr Sklenář (Chief Economist at J&T Bank). Jakub Seidler and Miroslav Zámečník contributed to the forecast on behalf of the CBA.

**For more information, please contact:**

Andrea Trudičová

CBA's PR and Communications

andrea.trudicova@cbaonline.cz

tel: + 420 734 638 103

**About the Czech Banking Association**

The Czech Banking Association was established in 1990; it is a voluntary association of legal entities operating in banking. It currently associates 37 members. The role of the Association is to represent and promote the common interests of its members in the first place, to present the role and the interests of banking towards the public, to participate in creating standard procedures and professional practices in banking, to support the harmonization of the banking laws with the EU legislation and to develop activities in disseminating information and in education. The CBA is a member of the European Banking Federation and of EMMI.