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Weekly Briefing

Czech Economy briefing:

Economy Outlook in Czech Republic in 2018

Zuzana Stuchlíková

China-CEE Institute

Kiadó: Kína-KKE Intézet Nonprofit Kft.

Szerkesztésért felelős személy: Chen Xin

Kiadásért felelős személy: Huang Ping

1052 Budapest Petőfi Sándor utca 11.

+36 1 5858 690

office@china-cee.eu

china-cee.eu

ECONOMIC OUTLOOKS FOR 2018

The outlooks for 2018 indicate that the Czech economy will continue to rise steadily (growth is projected to remain above 3%), which is closely connected to solid growth projections for the European Union countries and the entire global economy, driven especially by a strong growth in emerging economies and the U.S. economy. The overall economic situation of the Czech Republic should be positive. The private investment and household consumption is expected to grow dynamically in 2018 and 2019, thanks to "*wage dynamics reflecting low unemployment rate, high participation rate and record-high number of job vacancies*". Private investments and public infrastructure sending will be supported by funds from the European Structural and Investment Funds awarded under the 2014-2020 programme and still low real interest rates (Ministry of Finance 2017b).

The Czech fiscal policy is supposed to stay expansionary, with a positive effect on economic activity in the short run. As for the monetary policy, the Czech National Bank started to increase interest rates to 0.5 percent by the end of 2017 and continued in January 2018 (there was a 25 basis point interest rate hike). This tightening of monetary policy is necessary to keep inflationary expectations fixed. The Czech National Banks wants to raise interests rates gradually over time and normalise its policy.

The next economic policy will depend on the new government structure after the general elections in the Czech Republic in October 2017, won by a movement ANO. At the beginning of January 2018, the new Prime Minister Babiš´s government approved a new programme with six main points. Mr. Babiš would like: 1) to digitalise the Czech Republic; 2) be visible within Europe; 3) to increase government spending on infrastructure projects; 4) to implement pension´s reform; 5) to reform public finances; and 6) to increase security. Important fiscal reforms are included in this programme, especially higher public sector wages, a cut in value added tax in hospitality sector (from 21% to

15%), cuts in personal income and corporation taxes. These measures could further support household consumption and stimulate private and public investment.

Main short-term risks to the above projections include developments in the labour market (ongoing labour shortages, possible wage growth) and inflation pressures. The growth in interest rates in the Czech Republic (i.e. a rising interest rates differential between the Czech Republic and the Eurozone) could lead to further appreciation of the koruna with possible negative effects on Czech external competitiveness and foreign trade. And despite positive macroeconomic data from the Czech and European economy, some structural challenges remain – the Czech Republic shall invest more in human capital and infrastructure, boost labour supply and housing supply etc.