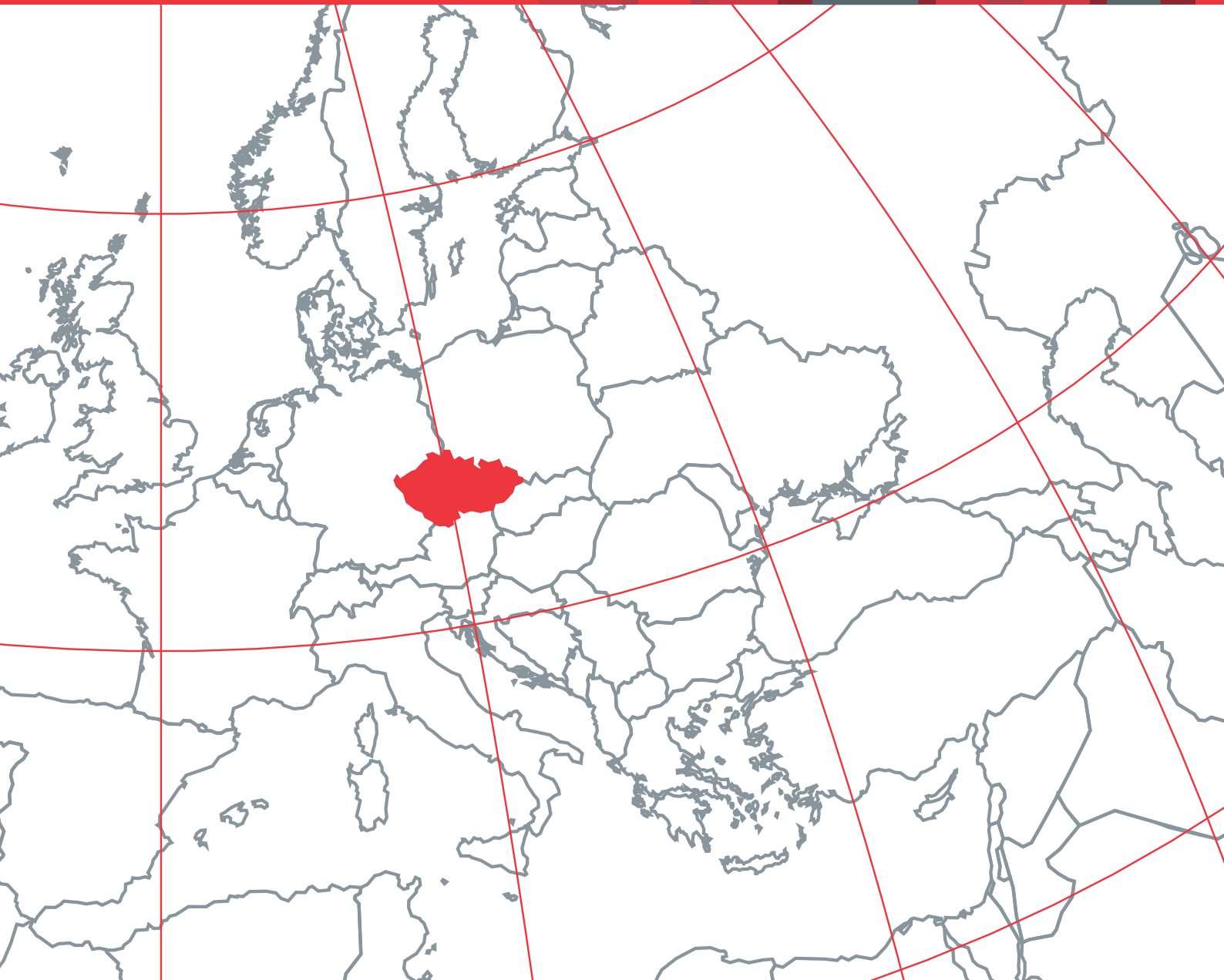


# Atradius Country Report

## Czech Republic – July 2013



# Czech Republic: Atradius STAR Political Risk Rating\*:

## 3 (Good) – Negative

\* The STAR rating runs on a scale from 1 to 10, where 1 represents the lowest risk and 10 the highest risk.

The 10 rating steps are aggregated into five broad categories to facilitate their interpretation in terms of credit quality. Starting from the most benign part of the quality spectrum, these categories range from 'High Quality', 'Good', 'Adequate', 'Impaired' to 'Prohibitive Conditions', with a separate grade reserved for 'Off Cover'.

In addition to the 10-point scale, there are rating modifiers associated with each scale step: 'Positive', 'Stable', and 'Negative'. These rating modifiers allow further granularity and differentiate more finely between countries in terms of risk.

For further information about the Atradius STAR rating, please [click here](#)

## Overview

### General information

Capital:	Prague
Government type:	Parliamentary democracy
Currency:	Czech Koruna (CZK)
Population:	10.6 million

### Most important sectors (% of GDP, 2012)

Services:	60.3 %
Industry/mining:	38.1 %
Agriculture:	1.6 %

### Main import sources (2012, % of total)

Germany:	25.2 %
China:	11.1 %
Poland:	7.1 %
Slovakia:	6.0 %
Russia:	5.6 %

### Main export markets (2012, % of total)

Germany:	31.4 %
Slovakia:	9.0 %
Poland:	6.1 %
France:	5.1 %
UK:	4.8 %

### Key indicators

	2010	2011	2012	2013*	2014*
Real GDP growth (y-on-y, % change)	2.3	1.8	-1.2	-0.8	2.1
Consumer price inflation (y-on-y, % change)	1.4	1.9	3.3	1.5	1.6
Real private consumption (y-on-y, % change)	0.9	0.5	-2.6	1.2	1.4
Retail sales (y-on-y, % change)	-2.0	0.7	-3.8	-0.9	-0.2
Industrial production (y-on-y, % change)	8.6	5.9	-0.7	0.0	4.5
Unemployment rate (%)	7.3	6.7	7.0	7.2	7.1
Real fixed investment (y-on-y, % change)	0.7	0.4	-2.6	-1.4	2.2
Export of goods and non-factor services (y-on-y, % change)	15.0	9.6	4.2	1.6	2.8
Real net exports (EUR billion)	6.9	9.9	12.1	11.6	10.1
Fiscal balance (% of GDP)	-4.8	-3.3	-4.4	-2.8	-2.9

\* forecast

Source: IHS Global Insight

# Political situation: Uncertainty has increased since Prime Minister Necas' resignation

Head of state: President Milos Zeman (since March 2013)  
Head of government: Prime Minister Jiri Rusnok (since July 2013)  
Form of government: Caretaker government

Uncertainty continues to characterise the Czech domestic political landscape. On 17 June 2013 Prime Minister Petr Necas resigned after prosecutors charged his chief of staff with corruption and abuse of power, precipitating the end of the ruling centre-right coalition. President Zeman refused to appoint the coalition's replacement candidate, Miroslava Nemcova, the parliamentary speaker. Instead he nominated a confidant, former finance minister Jiri Rusnok as successor, with the task of forming a caretaker government of technocrats.

This caretaker government was sworn in July 10th, and will face a vote of confidence, which must take place within 30 days of its appointment. It is most probable that it will lose this vote, as both the former centre-right coalition parties and even parts of the social democratic opposition oppose the president's move. However, even in case of a lost confidence vote the new government could stay in office, as president Zeman has no constitutional deadline to name a replacement before the next scheduled elections in May 2014. But any legislative proposals or initiatives made by the government are then likely to be opposed by MPs from the former coalition. This could also affect budget planning for 2014, limiting non-mandatory spending at 2013 levels.

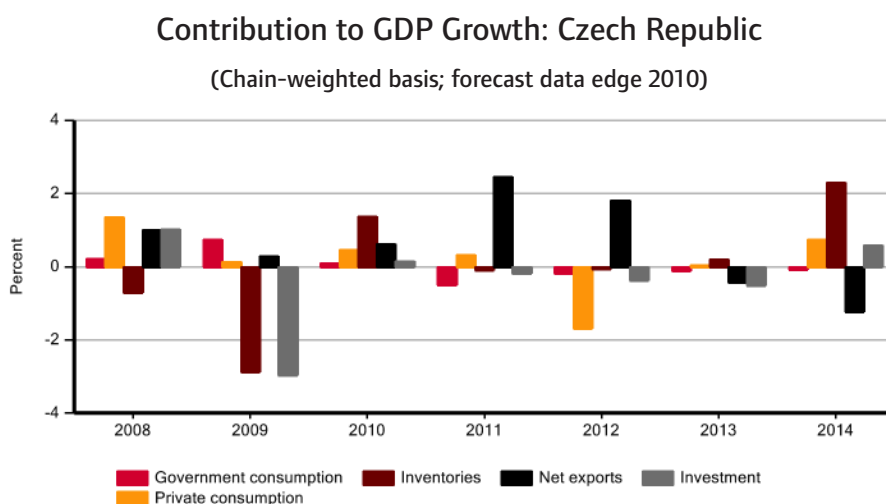
# Economic situation: GDP expected to contract again this year

## Decreasing domestic demand and lower exports in 2013

After a 1.2% year-on-year contraction in 2012, the Czech economy continued to shrink in early 2013: by 2.2% year-on-year in Q1 (down 1.1% on the previous quarter), with GDP forecast to decrease 0.8% in 2013.

The continued weak economic performance is partly the result of austerity measures. Tax increases and public sector cuts have lessened the purchasing power and confidence of both households and businesses, with a consequent impact on domestic demand. Private consumption is expected to increase only slightly – by 1.2% - this year after a 2.6% decrease in 2012, while lower government spending will continue to have a negative effect on growth. Industrial production will level off this year after a drop in 2012, investments will continue to decrease.

At the same time, low demand from EU trading partners will continue to hit exports. At more than 75%, the Czech Republic' export-to-GDP ratio is one of the highest in the EU, making it especially vulnerable to trade losses. The contribution of net exports to GDP will turn negative in 2013 (see chart below) as Eurozone growth shrinks by 0.7%.

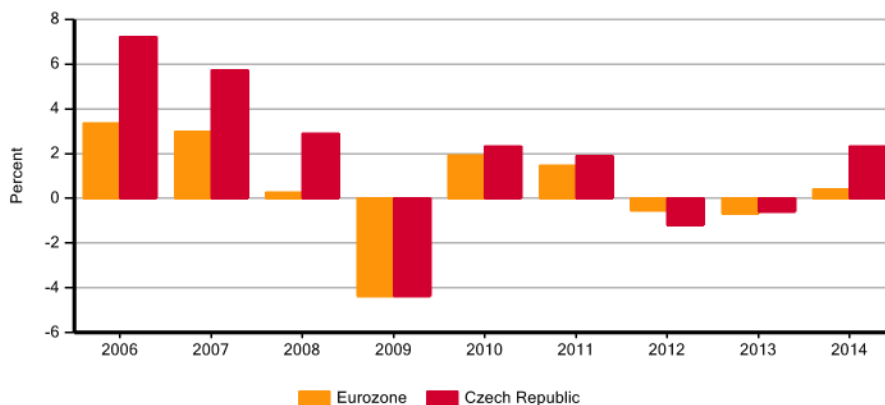


Source: IHS Global Insight

Despite this, economic growth is forecast to rebound significantly next year: by more than 2 % (see chart below), partly on the back of stronger demand from abroad, improving private consumption and rising investment. However, this anticipated recovery depends on a general improvement across Europe and increasing demand for goods from overseas.

### Real GDP growth

(Annual percentage change in real GDP; forecast for 2011 and 2012)



Source: IHS Global Insight

### Inflation to decrease in 2013

While inflation has been modest in recent years (1.9% in 2011), it rose to 3.3% in 2012 because of a VAT increase. However, since the end of 2012 – and as the effects of that VAT increase have faded – consumer prices have begun to drop and are now in line with the Eurozone average (see chart below). With lower inflation expected, and to support both domestic and foreign demand in the current difficult economic environment, the Czech Central Bank has cut the benchmark interest rate to a record low of 0.05%.

### Consumer price inflation

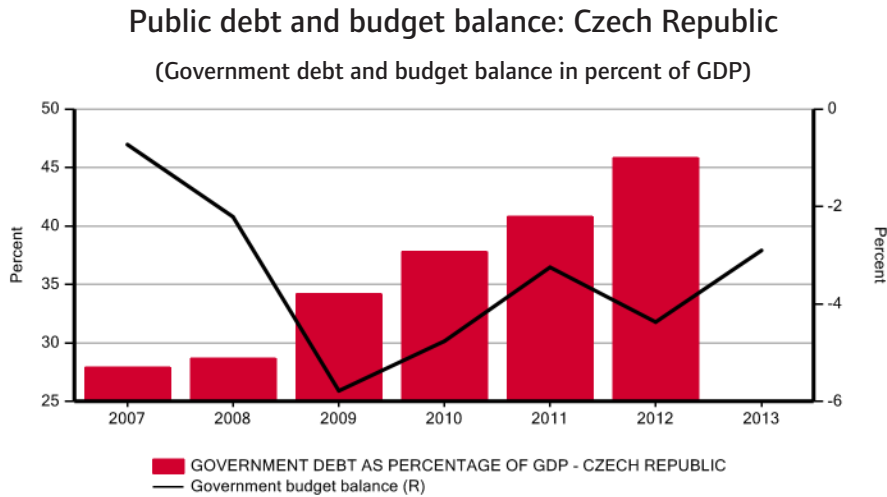
(Annual percentage change)



Source: IHS Global Insight

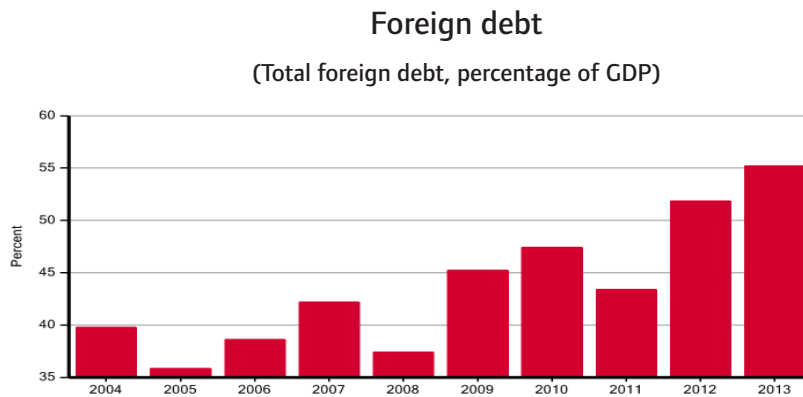
### Budget deficit forecast to drop below 3 % of GDP in 2013

Public finances are looking better, now that the budget deficit is expected to drop below 3 % of GDP this year for the first time since 2008 (see chart below), thanks to austerity measures taken by the former government. This should also stabilise the public debt-to-GDP ratio, which reached 48% of GDP in 2012 - up from 28% of GDP in 2007. While government debt is likely to increase further in the coming two years, the level should then stabilise at a sustainable rate.



Source: IHS Global Insight

The level of foreign debt has increased since 2011, but remains modest at around 55 % of GDP (see chart below).



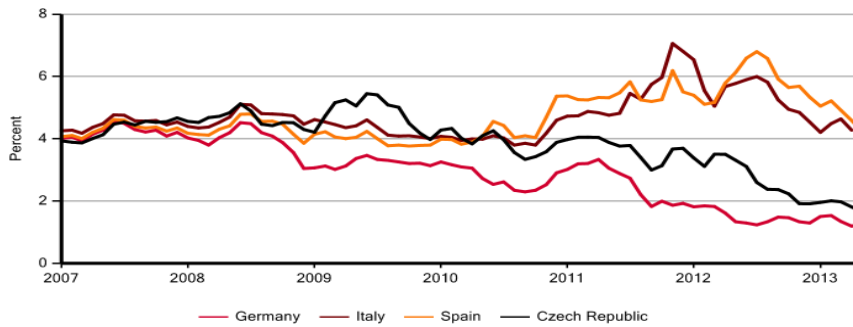
Source: IHS Global Insight

### Bond yields have decreased

International financial markets have a generally positive view of the Czech Republic, and government bond yields have decreased sharply over the past year (see chart overleaf). There are a number of reasons for this: the European Central Bank's announcement of support in the event of an escalation of the Eurozone crisis; the Czech Republic's economic policy - especially that aimed at cutting the budget deficit; and the fact that public finances are now in reasonably good shape. Lower yields make it cheaper for the government to (re)finance its debt, and therefore lower the pressure on the public purse.

## 10-year government bond yields

(Yields in percent per annum)



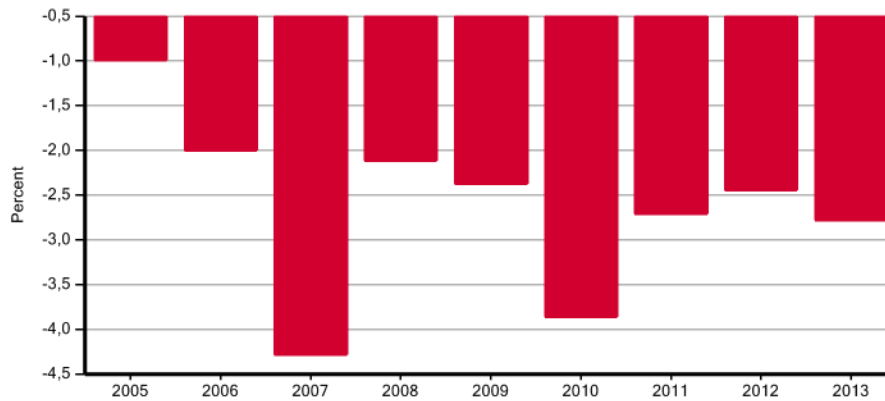
Source: IHS Global Insight

### Small current account deficit

The current account recorded a small deficit of 2.5% of GDP in 2012 and is forecast to increase slightly - to 2.9% of GDP - this year. Lower exports, due to weaker demand across Europe, are offset by a similar decrease in demand for imports. As both are expected to increase again in 2014, the effect on the current account will be kept in balance.

## Current account balance: Czech Republic

(Current account balance in percent of GDP)



Source: IHS Global Insight

### Some exchange rate fluctuations

After its high in mid-2008, the koruna exchange rate against the euro fell by around 10%. However, this was more a reflection of weakened market sentiment towards the whole Eastern European region than a negative perception of the Czech Republic itself. Since then, tensions have abated, although the exchange rate against the euro has fluctuated somewhat over the past twelve months. Despite some vulnerability to global market sentiments, we do not expect the koruna to fall victim to extreme volatility.

**Exchange rate Koruna per Euro**  
(Daily spot market rate)



Source: IHS Global Insight

## Czech Republic industries performance outlook

July 2013

Agriculture	Automotive/Transport	Chemicals/Pharma	Construction	Construction Materials
Consumer Durables	Electronics/ICT	Financial Services	Food	Machines/Engineering
Metals	Paper	Services	Steel	Textiles

Excellent  
 Good  
 Fair  
 Poor  
 Bleak

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