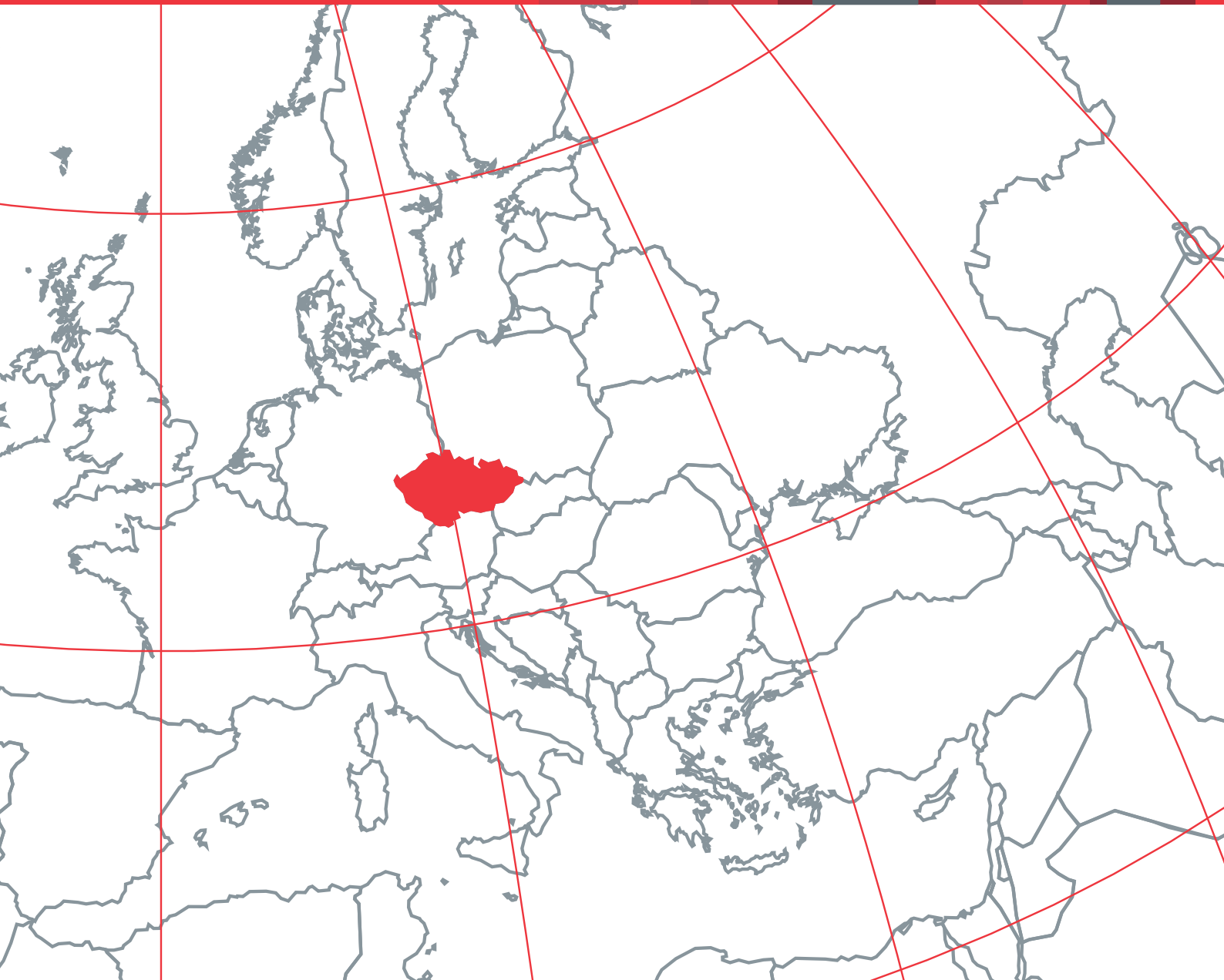


Atradius Country Report

Czech Republic – July 2014



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:	10.5 million

Most important sectors (% of GDP, 2013)

Services:	60.3 %
Industry:	37.3 %
Agriculture:	2.4 %

Main import sources (2013, % of total)

Germany:	30.4 %
Poland:	8.2 %
Slovakia:	7.3 %
China:	5.9 %
The Netherlands:	5.5 %

Main export markets (2013, % of total)

Germany:	31.3 %
Slovakia:	8.9 %
Poland:	6.0 %
France:	4.9 %
UK:	4.8 %

Key indicators

	2011	2012	2013	2014*	2015*
Real GDP (y-on-y, % change)	1.8	-0.9	-0.9	2.5	2.8
Consumer price (y-on-y, % change)	1.9	3.3	1.4	0.6	2.2
Real private consumption (y-on-y, % change)	0.5	-2.1	0.1	1.7	2.7
Retail sales (y-on-y, % change)	0.7	-3.8	-1.1	4.2	0.8
Industrial production (y-on-y, % change)	5.9	-0.8	-0.1	5.8	5.5
Unemployment rate (%)	6.7	7.0	6.9	6.5	6.0
Real fixed investment (y-on-y, % change)	0.4	-4.3	-3.6	4.6	4.1
Export of goods and non-factor services (y-on-y, % change)	9.6	4.7	0.2	8.6	3.7
Real net exports (EUR billion)	7.9	10.5	10.1	10.2	10.5
Fiscal balance (% of GDP)	-3.2	-4.2	-1.5	-1.8	-2.3

* forecast

Source: IHS Global Insight

Political situation: More stability with a new government

Head of state: President Milos Zeman (since March 2013)
Head of government: Prime Minister Bohuslav Sobotka (since January 2014)

In June 2013 Prime Minister Petr Necas of the centre right party ONS 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, and instead nominated a confidant, former finance minister Jiri Rusnok, as successor. He was given the task of forming a caretaker government of technocrats, which was sworn in in July 2013. However, this caretaker government lost a vote of confidence in August, as the former centre-right coalition parties opposed the president's actions. Also in August, the Chamber of Deputies finally passed a motion dissolving itself, paving the way for snap elections in October.

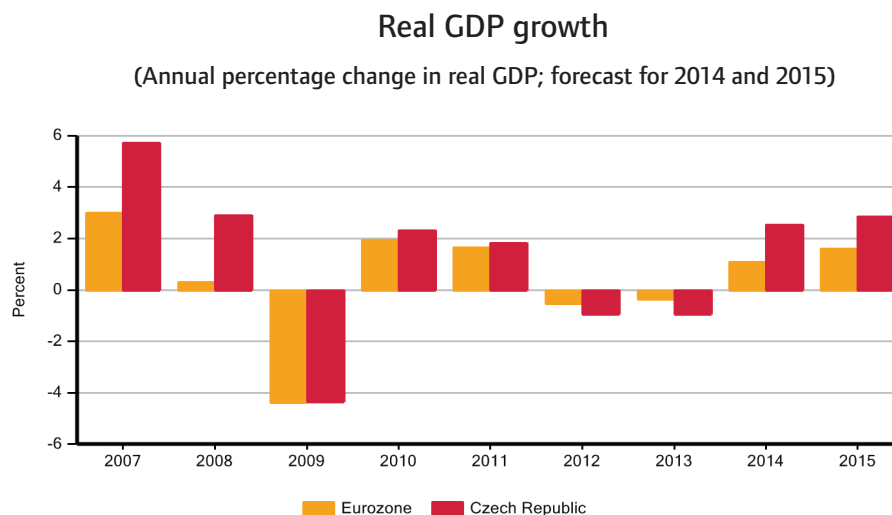
As a result of those October elections, a centre left-coalition was established, holding 111 of the 200 seats in parliament. The coalition is led by the leftist Czech Social Democratic Party (CSSD), while the other two parties in the coalition are the centrist ANO 2011 and the Christian Democrats (KDU-CSL). The new government was finally sworn in in January 2014.

Economic situation: Growth has returned

A broad-based rebound

After a 0.9% year-on-year contraction in 2012, the Czech economy continued to shrink in 2013: again by 0.9%. This weak economic performance was partly the result of austerity measures, as tax increases and public sector cuts lessened the purchasing power and confidence of both households and businesses, with a consequent impact on domestic demand. At the same time, last year low demand from EU trading partners hit exports. At more than 75%, the Czech Republic's export-to-GDP ratio is one of the highest in the EU, making it especially vulnerable to foreign trade losses. The contribution of net exports to GDP turned negative in 2013 as Eurozone growth shrank 0.4%.

However, the economy has picked up since the end of 2013, growing 2.5% year-on-year in Q1 of 2014. The Czech economy is forecast to grow about 2.5% in 2014 and 2.8% in 2015.

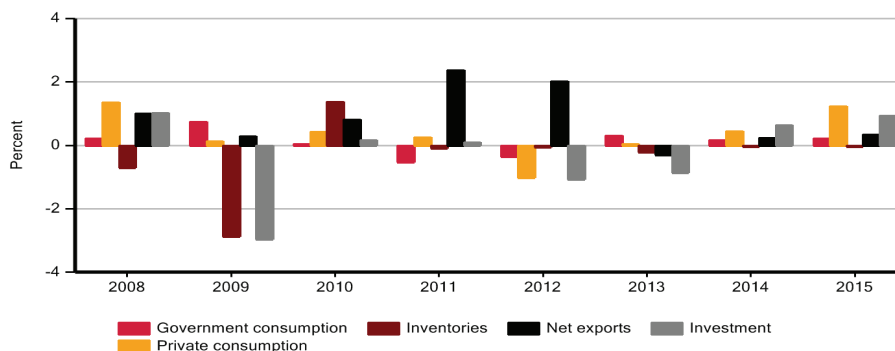


Source: IHS Global Insight

This recovery is expected to be broad-based, benefiting from rising private consumption, investment and government spending (see chart below). Net exports are expected to pick up, due to the more benign economic conditions in the Eurozone and Germany's robust economic performance.

Contribution to GDP Growth: Czech Republic

(Chain-weighted basis; forecast data edge 2013)

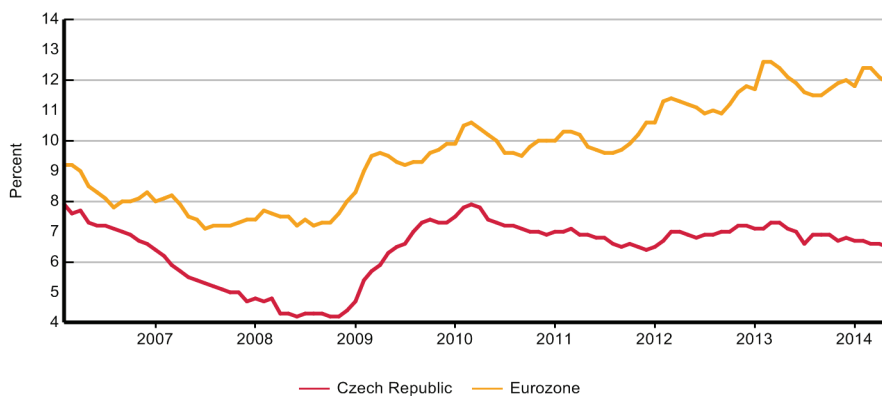


Source: IHS Global Insight

The Czech Republic's unemployment rate reached 6.5% in April 2014, down from 7.1% in April 2013. Its jobless rate is considerably lower than that of the Eurozone (see chart below) and, with the economy gaining strength, unemployment is expected to decrease further, to 6.0% in 2015.

Unemployment rate

(ILO definition, NSA, percent)



Source: IHS Global Insight

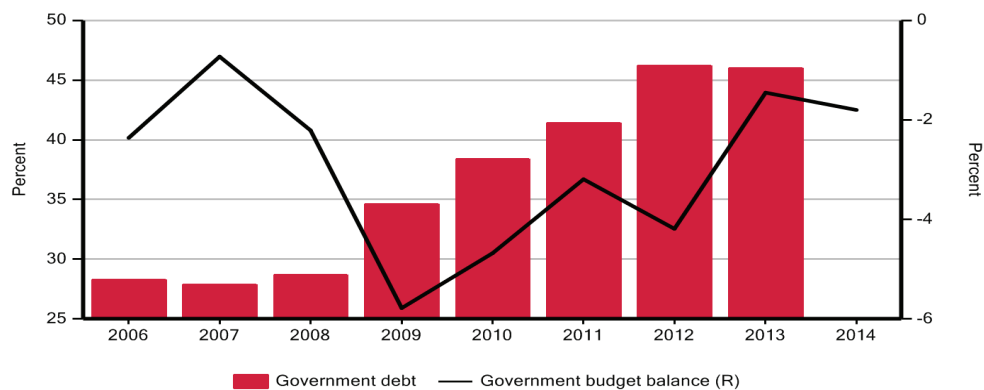
Budget deficit dropped below 3% of GDP in 2013

Despite the economic contraction, government finances improved in 2013 as the budget deficit decreased from 4.2 % of GDP in 2012 to just 1.5 %, putting it below the 3 % of GDP Maastricht threshold. In 2014 the budget deficit is expected to remain below this threshold, at around 1.8 % of GDP. As a result of the latest deficit reduction, the European Commission has decided to remove the Czech Republic from its Excessive Deficit procedure under which EU member states are obliged to avoid excessive deficits in their national budgets.

Government debt decreased slightly in 2013, to 46 % of GDP, but remains moderately high, after the public debt-to-GDP ratio reached 46.2 % of GDP in 2012 – up from 28 % of GDP in 2007. Government debt is expected to remain stable or even to improve slightly in 2014.

Public debt and budget balance, Czech Republic

(Government debt and budget balance in percent of GDP)

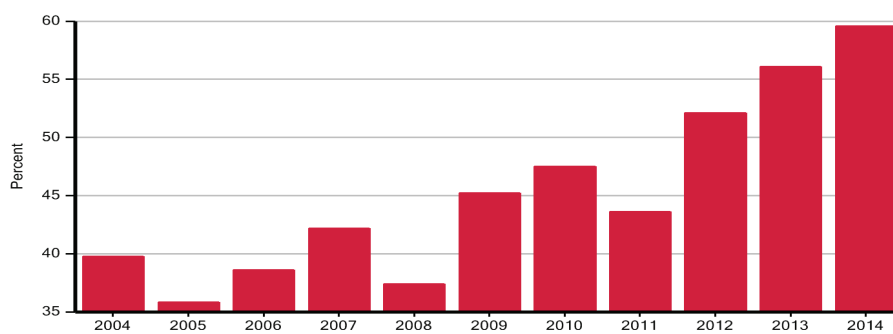


Source: IHS Global Insight

The level of foreign debt has increased since 2011: from 42 % of GDP in 2007 to 56 % of GDP in 2013. However, even with another expected increase in 2014, to 59.6 % of GDP, the Czech Republic's foreign debt remains manageable.

Foreign debt

(Total foreign debt, percentage of GDP, forecast 2014)



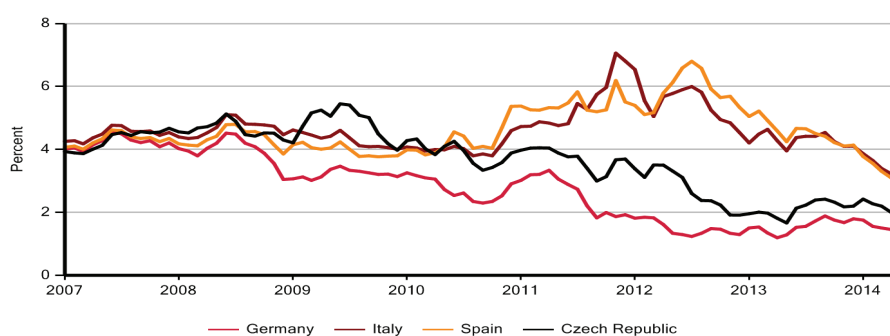
Source: IHS Global Insight

Favourable financial market conditions

International financial markets have a generally positive view of the Czech Republic. The yield on 10-year government bonds increased in June 2013, because of heightened political uncertainty following the resignation of Prime Minister Necas and the appointment of a caretaker government, but has decreased since the end of 2013 (see chart below). This reflects prudent Czech economic policy – especially that aimed at cutting the budget deficit - and the fact that public finances are now in reasonably good shape. In May 2014 the average yield was 1.73%: close to the German yield of 1.46%. Lower yields make it cheaper for the government to (re)finance its debt and therefore reduce pressure on the public purse.

10-year government bond yields

(Yields in percent per annum)



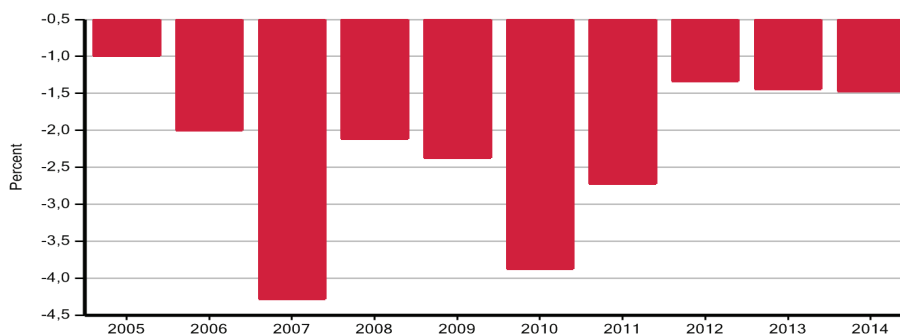
Source: IHS Global Insight

Small current account deficit

The current account recorded a small deficit of 1.4% of GDP in 2013 which is forecast to increase slightly – to 1.5% of GDP – this year. The current account benefits from improving export performance, as demand from Germany and other European markets is picking up. However, this is offset by rising imports as domestic demand rebounds.

Current account balance: Czech Republic

(Current account balance in percent of GDP, forecast 2014)



Source: IHS Global Insight

Weakening the exchange rate to boost exports...

Despite some vulnerability to global market sentiments, we do not expect the koruna to fall victim to extreme volatility.

In order to improve Czech competitiveness and boost exports, in November 2013, the Central Bank intervened in the currency market by buying euros in order to weaken the koruna against the Euro. As a consequence the koruna fell from 25.7 to the euro to 27 to the euro over that month. The exchange rate has been stable in 2014, hovering around 27.4 koruna to the euro.

Exchange rate Koruna per Euro

(Daily spot market rate)



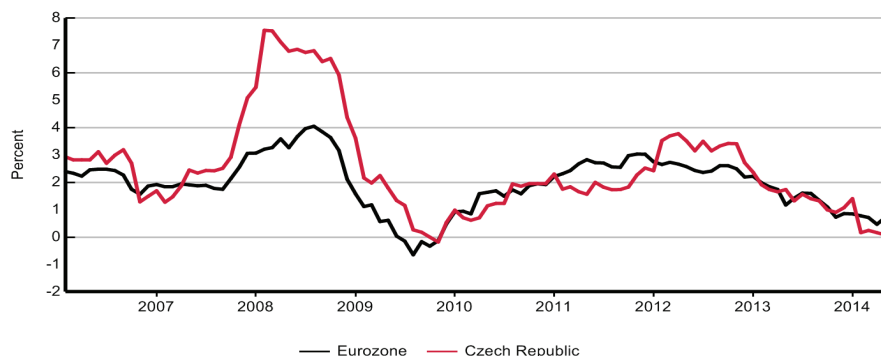
Source: IHS Global Insight

...and to combat deflation

A second objective of the Central Bank's intervention was to ward off deflation, as the koruna depreciation makes imports more expensive. Since the end of 2012 – and as the effects of a VAT increase have faded – consumer prices have begun to drop and are now in line with the Eurozone average (see chart below). Inflation reached only 0.5% in May 2014, far below Central Bank's target of between 1% and 3%. After increasing 0.6% in 2014, inflation is expected to increase 2.2% in 2015.

Consumer price inflation





















(Annual percentage change)



Source: IHS Global Insight

Czech Republic industries performance outlook

July 2014

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

Despite the current economic rebound, trading risks exist across a number of Czech trade sectors, as they do in all markets. Many companies minimise these risks to their profitability by insuring their credit sales with Atradius.

You can find out more about the ways in which we can protect the sales that you make on credit terms, [on the Atradius website](#).

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Atradius Credit Insurance N.V

Postbus 8982
1006 JD Amsterdam
David Ricardostraat 1
1066 JS Amsterdam
www.atradius.com