

## 2. Macroeconomic development

### 2.1. Performance of economy<sup>1</sup>

- **The Czech economy slowed significantly in 2008**

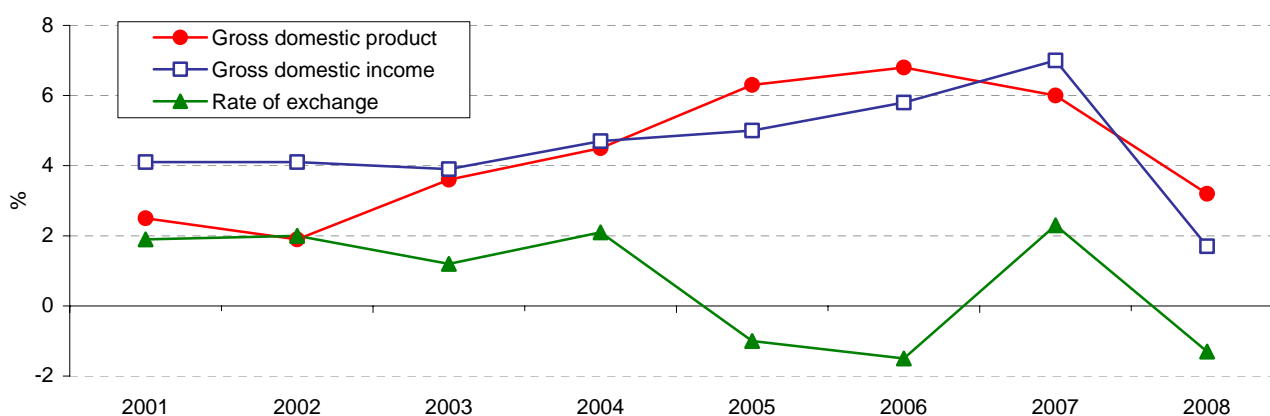
The real consequences of the financial crisis in the form of the economic slowdown of the most significant economies continuing from 2007 had a substantially negative impact on the Czech economy. The pace of the year-on-year increase in GDP was relatively high starting from 2001. Its growth admittedly slowed slightly in 2002, but from the start of 2003 it gradually increased every year up to the highest growth rate achieved in 2006. 2006 represented the peak in that growth phase of the economy, although the terms of trade negatively affected the development of the gross domestic product from the point of view of the external relations. 2007 still belonged to the period of relatively strong economic growth from the point of view of the aggregate national economic results, although there was a slowdown in the pace of GDP growth in the second half of the year. National work increased in value significantly in the international markets, which led to a significant acceleration of the growth of the gross domestic income.

The growth in GDP lost its dynamic in 2008 and it only grew by 3.2% and thus fell by less than half in comparison with the previous year. In comparison with the average year-on-year growth rate from 2001 to 2007, this was 1.3 percentage points less. This fact was the consequence of unfavourable internal and external facts, a fall in domestic and international orders and the insufficient sales of products on the internal and external markets. During the course of 2008, there were exceptional, unequal fluctuations in the individual GDP components. The swiftness and strength which came to bear on the changes in the GDP growth rate, the components of the gross domestic final expenditure and the exports and imports in the individual quarters of 2008 had no predecessors in the previous development.

- **The growth in the gross domestic income was slower than the growth in GDP**

In 2008, the terms of trade worsened (they fell by 1.3% year-on-year) which was caused by the rapid reduction of the year-on-year growth of the gross domestic income to 1.7% and its year-on-year change therefore did not reach the medium-term average for the period from 2001 to 2007 (4.9%). For the Czech Republic, the slightly more favourable development of income, expenditure and capital transactions abroad led to the fact that the gross national disposable income with a year-on-year increase of 5.1% at current prices exceeded the value of the nominal growth of GDP (5%).

**Graph 2.1.1** Gross domestic product, gross domestic income (in %, year-on-year, constant prices 2000) and the terms of trade (in %, year-on-year)



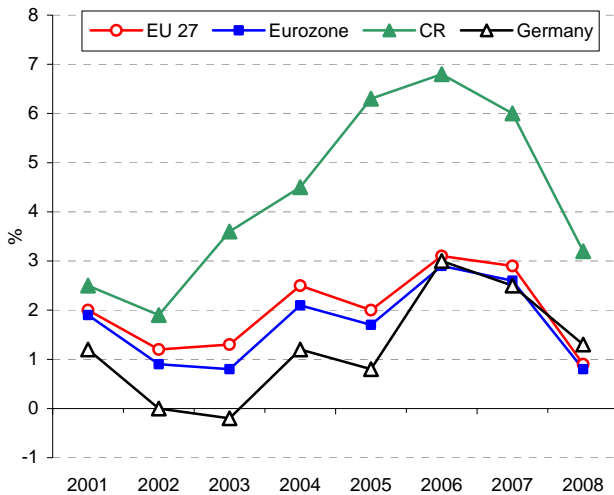
Source: the Czech Statistical Office

- **GDP per capita in PPP remained at the level of 80.2% of the average for the EU 27**

The gap between the Czech economy and the economy of the EU 27 in the outputs measured by the growth in GDP at constant prices amounted to 2.3 percentage points in 2008. According to Eurostat, the share of the Czech Republic in the EU 27 during the calculation of GDP per capita in purchasing power parity did not change from 2007 and it remained at 80.2%.

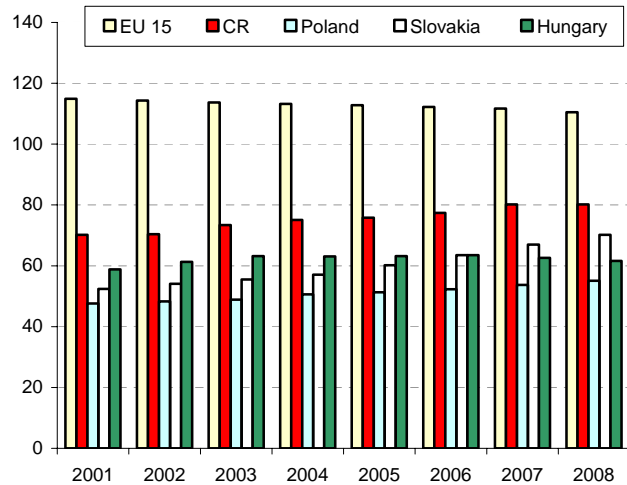
<sup>1</sup> The information stated in this section has not been seasonally adjusted, unless stated otherwise.

**Graph no. 2.1.2 Gross Domestic Product**  
(in %, year-on-year, constant prices 2000)



Source: Eurostat

**Graph no. 2.1.3 Gross Domestic Product per capita<sup>2</sup>**  
(in PPS, EU 27 = 100)



Source: Eurostat

## Demand side of the economy

- Households curbed their expenditure on final consumption**

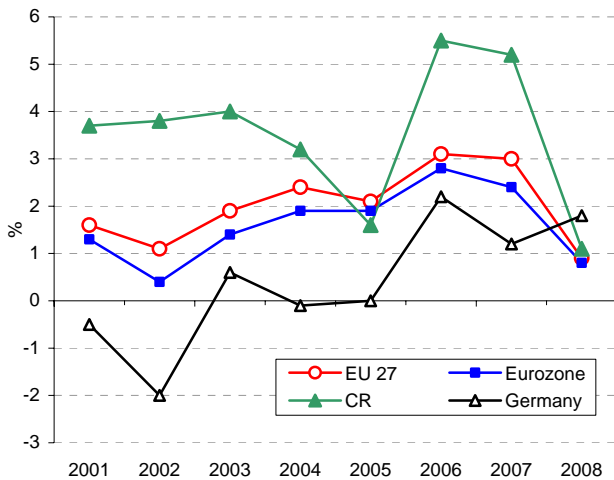
The growth in the gross domestic final expenditure<sup>3</sup> in the Czech Republic slowed year-on-year to 1.1%, although it was 5.2% in the previous year. This constituted a significant loss of vitality from the medium-term point of view of the average growth in the period from 2001 to 2007, which amounted to 3.9%. The growth in household consumption fell by almost one half from 5.2% to 2.9% in 2008 and this amount was also under the average for the period from 2001 to 2007 (3.8%). The expenditure on household final consumption was negatively influenced by the low growth of real wages by just 2.1%, which was the lowest value since 1998.

The increased inflation not only led to slower growth in real wages, but also to a loss of value in the population's savings. The tightening up of the conditions for the provision of consumer and mortgage loans further reduced the options for financing household expenditure using external funds. The year-on-year growth in the value of the aggregate deposits in household bank accounts, the largest in the last six years (144.8 billion CZK), bore witness to the fact that people also saved more from this point of view. These facts together with the risk of the loss of employment stood behind the reduction in household consumption. Consumers thus expected a worsening of their economic situation in the years to come.

<sup>2</sup> The data for 2008 was the Eurostat forecast.

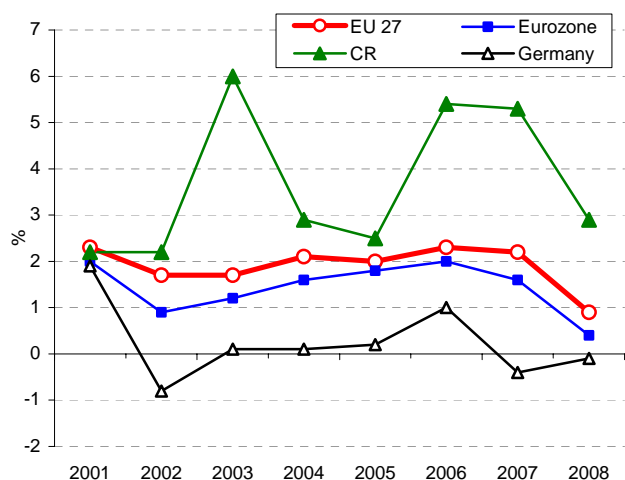
<sup>3</sup> The gross domestic final expenditure is calculated as the sum of the expenditure outlaid on the final consumption of households, non-profit organisations and the government and the creation of gross capital.

**Graph no. 2.1.4 Gross domestic final expenditure**  
(in %, year-on-year, constant prices 2000)



Source: Eurostat

**Graph no. 2.1.5 The consumption of households and non-profit institutions**  
(in %, year-on-year, constant prices 2000)



Source: Eurostat

- ***The government slightly increased its expenditure***

Even though the rate of growth in government consumption increased year-on-year from 0.4% in 2007 to 0.9%, the government managed to reduce its expenditure in the medium-term horizon, because the average year-on-year growth in the period from 2001 to 2007 amounted to 2.3%. Like households, the government also cut down on its expenditure on final consumption.

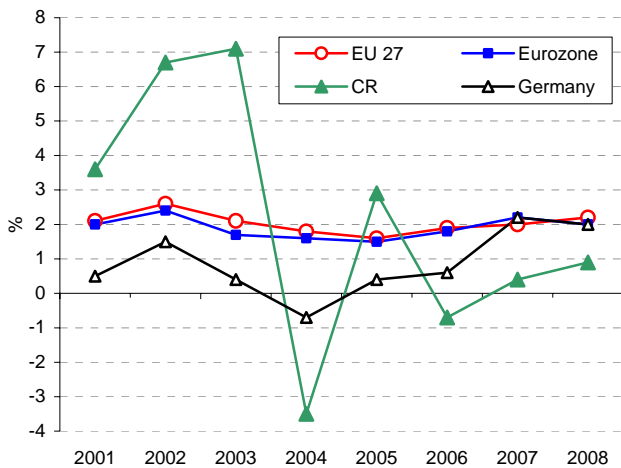
- ***Company investments fell in absolute terms ...***

As a consequence of the unfavourable internal and external investment environment and the weakening foreign demand, company investment activities within the territory of the Czech Republic fell significantly. Gross capital formation fell by 1.4% year-on-year in 2008, which was the worst result since 1999. The average from the period from 2001 to 2007 was much higher (5.2%). The size of the investments was also influenced by the negative prospects for businesspeople in the years to come and their subjective perception of a lack of funds as a consequence of the increased caution of the banks which were afraid of their clients becoming insolvent.

- ***... mainly thanks to the lower change of inventory***

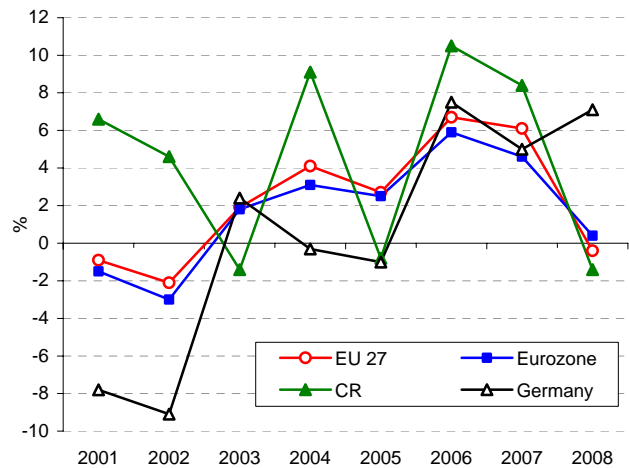
Gross fixed capital formation (GFCF) increased by 3.1%, which was 1.3 percentage points less than the average for the period from 2001 to 2007. The lower changeover in company inventories particularly contributed to the slump in gross capital formation. The material structure of the gross fixed capital formation (at current prices) changed slightly in favour of means of transport and other machines and equipment in 2008. Their share of the GFCF increased from 41.4% in 2007 to 42.2% in 2008, whereby both of these components rose. On the other hand, less was invested in housing and other buildings and structures, whose share fell from 53.4% to 52.5%. The share of housing investments in the GFCF fell significantly (by 1.6 percentage points), while on the other hand the share of investments in other buildings and structures increased (by 0.6 percentage points). The investment of households in new housing was limited not only by the tightening up of the provision of loans by the banks, but also by the bad prospects for future economic developments and also by speculation that the price of the real estate would fall.

**Graph no. 2.1.6 Government consumption**  
(in %, year-on-year, constant prices 2000)



Source: Eurostat

**Graph no. 2.1.7 Gross capital formation**  
(in %, year-on-year, constant prices 2000)



Source: Eurostat

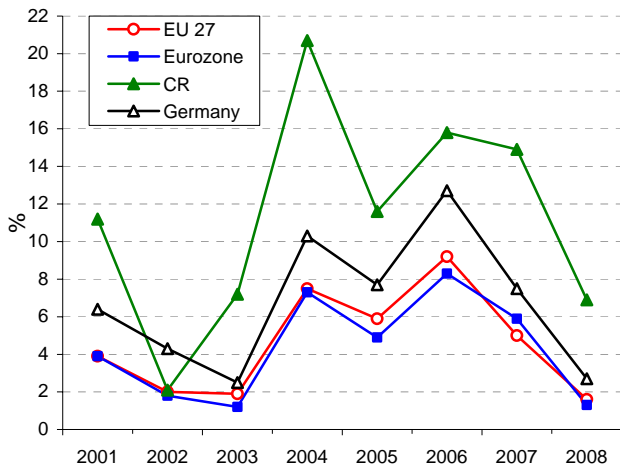
- **The recession experienced by our commercial partners reduced exports ...**

The recession in the economies of the most significant commercial partners and therefore also the slowdown in foreign demand, which was especially apparent in the slump in the export branches of the processing industry, was only slightly compensated for from the point of view of Czech exports by the depreciation of the exchange rate in the second half of 2008. The depreciation of the exchange rate for the crown partially attenuated the fall in the prices for inputs – commodities traded in world markets. The terms of trade significantly worsened in 2008 precisely under the influence of the development of world prices and the exchange rate. Whereas the growth rate for exports of goods and services had been in double digits for the previous four years, 2008 brought a year-on-year growth of just 6.9%, which was almost 5 percentage points lower than the average for the period from 2001 to 2007. The relatively low growth in the export of goods (5.7%) in combination with the acceleration of the growth in the export of services (15.1%) significantly contributed to this low growth rate.

- **... and brought changes to their territorial and goods structure**

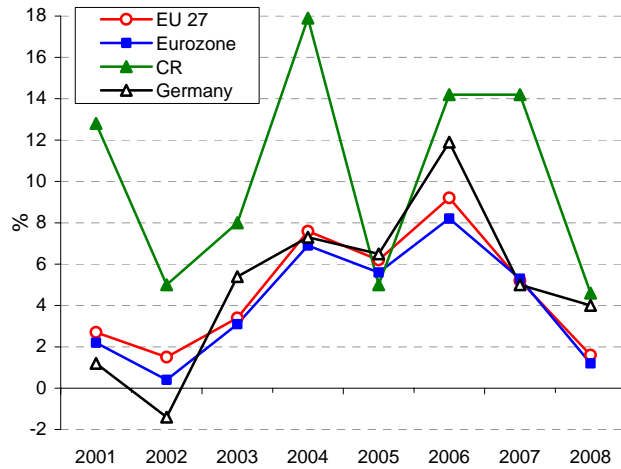
The economic slowdown in the main commercial countries especially manifested itself in the territorial structure of the foreign trade. Exports fell most year-on-year to Great Britain (6.5%), France (2.1%) and Germany (0.5%). Exports to the countries of the EU 27 fell by 0.8% which meant a slight reduction of their share in the overall exports of the Czech Republic by 0.2 of a percentage point to 85.1%. On the other hand, companies most succeeded in increasing exports to the surrounding countries such as Poland (8.0%) and Slovakia (6.3%). The slowdown in the processing industry also influenced a change in the commodity structure of exports. The share of machines and means of transport in the total exports fell year-on-year by 0.7 percentage points to 53.5% and the share of semi-products and materials similarly fell by 0.5 percentage points to 19.7% in 2008. The position of machines and means of transport and semi-products and materials also weakened similarly in imports.

**Graph no. 2.1.8 Exports of goods and services**  
(in %, year-on-year, constant prices 2000)



Source: Eurostat

**Graph no. 2.1.9 Imports of goods and services**  
(in %, year-on-year, constant prices 2000)



Source: Eurostat

- **The Czech economy absorbed imports at a lower rate**

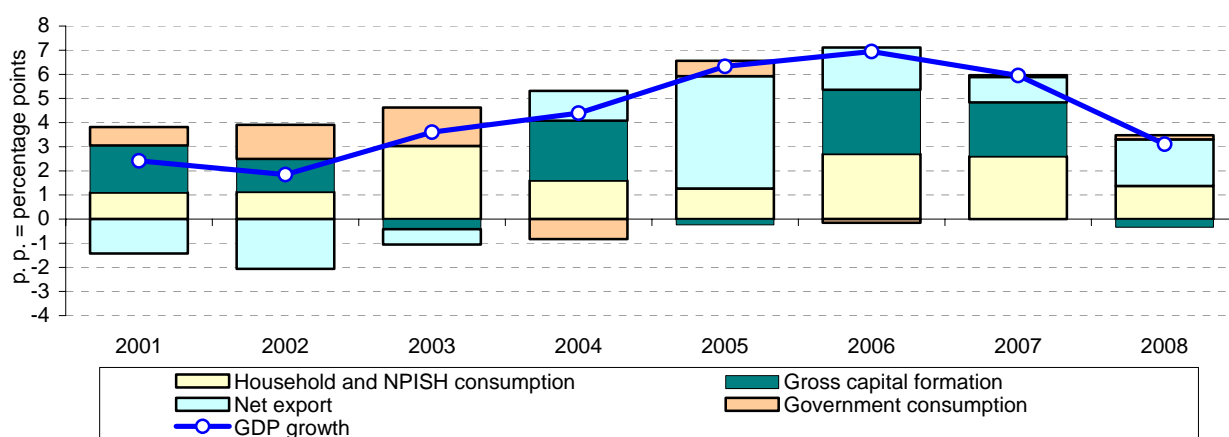
The fall in the growth rate for imports was caused by falling demand not only in Czech households, but mainly in Czech companies. Czech exports, especially the processing industry, are largely dependent on the import of raw materials which are processed within the territory of the Czech Republic and then exported. The weakening of the Czech crown in the second half of 2008, which caused imports to be more expensive, also played a role. The imports of goods and services to the Czech Republic increased year-on-year by 4.6%, which was 6.3 percentage points less in comparison with the average for the period from 2001 to 2007. As was also the case for exports, the growth rate for imports differed in the case of goods and services. The growth rate for the importation of services (7.9%) substantially exceeded the growth rate for the importation of goods (4.2%).

- **The growth in GDP was led by household consumption and net exports**

The seasonally adjusted GDP growth of 3.1%<sup>4</sup> was mainly supported by the net export of goods and services with a contribution at the amount of 1.9 percentage points, whereby exports supported the growth by 5.2 percentage points and imports reduced it again by 3.3 percentage points. A further driving force of economic growth was household consumption, the contribution of which amounted to 1.4 percentage points. The fall in investments (gross capital formation) negatively influenced the growth of GDP with a contribution of -0.3 percentage points. Within the framework of the gross capital formation, the growth in GDP was mainly reduced by the change in inventories (by 1.1 percentage points) which was not compensated for by the positive contribution to the gross fixed capital formation (0.7 of a percentage point). Government consumption contributed positively to the growth of GDP by 0.2 of a percentage point. In comparison with the medium-term averages achieved in the period from 2001 to 2007, most of the contributions demonstrated below average values. The average growth of household consumption between 2001 and 2007 reached 1.9 percentage points, while government consumption was 0.5 of a percentage point, gross capital formation accounted for 1.4 percentage points and gross fixed capital formation was 1.2 percentage points and changes in inventory amounted to 0.3 of a percentage point. The exception was net exports, the average of which in the period from 2001 to 2007 was 1.2 percentage points less than in 2008.

<sup>4</sup> The numerical disagreement between the growth in GDP and the sum of the contributors to its growth is caused by the method of numerical rounding.

**Graph 2.1.10 The contributions of the expenditure components to the growth of GDP (in percentage points, constant prices 2000, seasonally adjusted)**



Source: the Czech Statistical Office

### Supply side of the economy

**• Gross added value increased the most out of all the production characteristics in 2008**

The production performance of the Czech economy measured by the volume of produced goods and services, consumed intermediate products and created gross added value has dynamically increased throughout the monitored eight years and during the last four years the growth in production and intermediate consumption significantly increased in 2006, while the growth in gross added value did so in 2005. The peak growth in all three fundamental production characteristics was achieved in 2006; production by 10.0%, intermediate consumption by 11.5% and the gross added value by 7.1%. In 2007 and 2008, there was a reduction in the year-on-year growth in the gross added value. 2008 was a below-average year in the light of the average value for the period from 2001 to 2007. Production increased by 3.5% which was 2.9 percentage points less than the aforementioned average, while intermediate consumption also increased by 3.5% and its difference in relation to the average amounted to 3.9 percentage points. In 2008, the gross added value grew by 0.9 of a percentage point less than the medium-term average from the period of 2001 to 2007. The tempo of the year-on-year growth of all the indicators was relatively variable and the overall annual growth hides a number of larger or smaller deviations. The development of the intermediate consumption was subject to the largest degree of variability and this was partially influenced by the changes in the prices for the intermediate products purchased in international markets and from domestic production.

**Table no. 2.1.1 Production, intermediate consumption and gross added value**

	2001	2002	2003	2004	2005	2006	2007	2008
Production – billions of CZK, current price	5 874.0	6 033.2	6 385.4	7 059.4	7 437.0	8 318.0	9 058.0	9 374.2
PR = 100.0 from the constant price	107.3	103.1	105.1	106.8	105.3	110.0	107.1	103.5
Intermediate consumption - billions of CZK, current price	3 741.6	3 793.1	4 042.3	4 529.4	4 761.7	5 417.7	5 876.2	6 055.6
PR = 100.0 from the constant price	110.1	103.4	106.4	108.2	104.7	111.5	107.8	103.5
Gross added value - billions of CZK, current	2 132.4	2 240.1	2 343.1	2 529.7	2 675.3	2 900.3	3 181.8	3 318.6
PR = 100.0 from the constant price	102.5	102.5	102.9	104.5	106.6	107.1	105.8	103.6

Source: the Czech Statistical Office

- **The tertiary sector once again strengthened its position in the supply structure**

The structural branch movements of production, intermediate consumption and gross added value in the three fundamental branch groupings (sectors) roughly characterised the main changes which occurred in the monitored period. The secondary sector (and in that the processing industry) had the greatest weight in production. Given the fact that the share of intermediate consumption in production was highest in this sector and that the weight of this sector in intermediate consumption significantly exceeded its weight in production, its share of formation was significantly lower. The demands of the gross added value on the consumed intermediate product were highest in the secondary sector where it exceeded the average by almost one third. The tertiary sector had the lowest such demands.

Varying trends asserted themselves in the different sectors from the point of view of the structure of the supply side of the economy (gross added value). In the primary sector (agriculture, forestry, fishing – BCEA A+B), the weakness of the sector's share of the gross added value which had started in 2005 continued and it reached 2.3%, which was the lowest value in the monitored period. The share of the secondary sector (industry, mining and construction – BCEA C+D+E+F) fell under 38% after two years of increases. On the other hand, the tertiary sector (services – BCEA G to P) strengthened its position in the supply structure and it once again exceeded a 60% share of the gross added value after a five-year period.

**Table 2.1.2 The structure of the gross added value (in %, current prices)**

Sector	2001	2002	2003	2004	2005	2006	2007	2008
Primary	3.9	3.3	3.1	3.3	3.0	2.6	2.4	2.3
Secondary	37.7	36.7	35.9	38.6	37.9	38.2	38.9	37.6
Tertiary	58.4	60.0	61.0	58.1	59.1	59.2	58.7	60.1

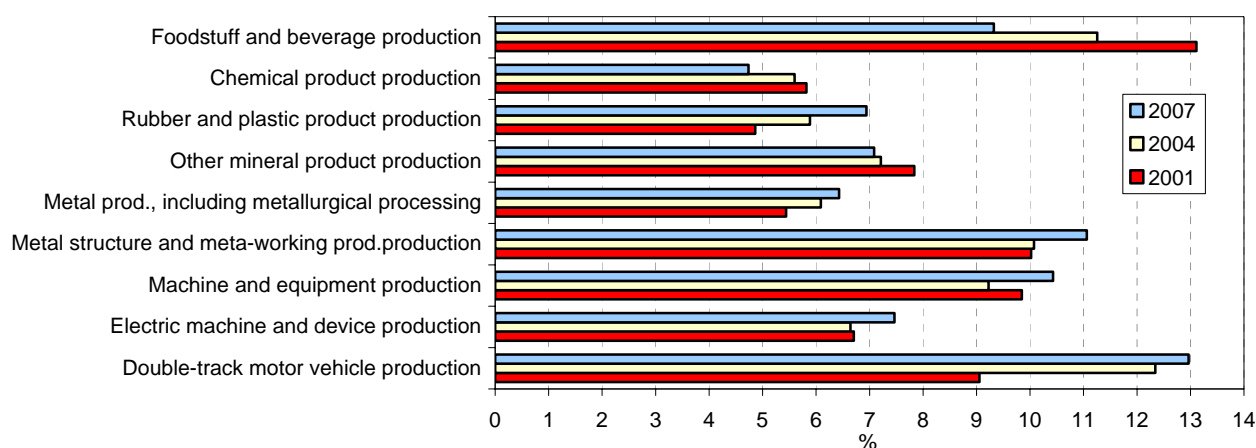
Source: the Czech Statistical Office

- **Significantly below-average growth in the processing industry**

The performance of the processing industry (gross added value) at constant prices in 2008 increased by 4.6%. However, this value was 3.2 percentage points lower in comparison with the average for the period from 2001 to 2007. The fall in the growth of the gross added value was caused by the declining external and internal demand. The reduction in domestic and especially foreign orders most affected the export oriented branches of vehicle production, the production of metals, metallurgical and metal-working products or the production of electrical and optical machines and equipment. Industry's production capacity was used to an increasingly lesser extent, starting from the end of 2007. On average, this was 87.5% for 2008, while it was 88.2% in the previous year.

The development of the structure of the gross added value bore witness to the changes in the performance of the individual branches which manifested themselves most in the processing industry. In 2007, the companies in the processing industry specialised more in the production of double-track motor vehicles in comparison with 2001 and this increased by 3.9 percentage points to 13% from the point of view of the share of the gross added value. The production of rubber and plastic goods or the production of metal structures and metal-working products strengthened more significantly by 2.0 percentage points to 6.9% and 1.1 percentage points to 11.1% respectively. On the other hand, the production of foodstuffs and beverages (a fall of 3.8 percentage points to 9.3%), chemical products (a fall of 1.1 percentage points to 4.7%) or other mineral products (a fall of 0.7 of a percentage point to 7.1%) declined in relation to the medium-term average.

**Graph 2.1.11 The share of the selected branches on the processing industry's gross added value (current prices)**



Source: the Czech Statistical Office

• ***The growth in the gross added value of services was the lowest since 2004***

In 2008, the gross added value in services rose by 4.3%, which meant the lowest year-on-year growth after 2002 and 2004. Only four of the ten branches were able to increase the gross added value at constant prices. This mainly involved the trading and repair of motor vehicles and consumption materials by 15.3%, which corresponded approximately to double the average for the period from 2001 to 2007, and also banking and insurance by 6.3% (the medium-term average amounted to 5.1%). On the other hand, the gross added value fell year-on-year in absolute terms in the branch of hospitality and accommodation by 0.2% (the average in the period from 2001 to 2007 amounted to -5.0%), transport, storage, postage and telecommunications by 0.5% (with an average of 5.6% for the period from 2001 to 2007) and real estate, services for companies and research and development by 0.9% (with a medium-term average of 3.8%).

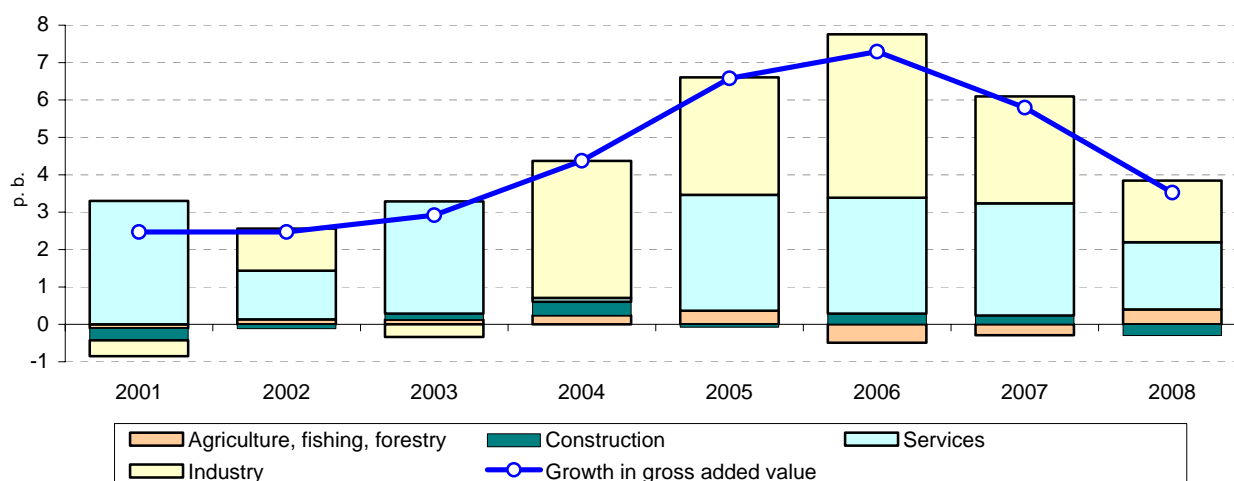
In a comparison of 2001 and 2008, the share of gross added value significantly increased in the case of banking and insurance from 5.6% to 6.4% or miscellaneous public, social and personal services from 4.9% to 5.6%. The representation of the branch of the trading and repair of motor vehicles and consumption materials increased slightly by 0.2 of a percentage point to 22.7% and real estate, services for companies and research and development increased by 0.4 of a percentage point to 23.2%. On the other hand, there was a medium-term reduction in the branch of hospitality and accommodation by -0.5 percentage points to 3.0% and transport, storage, postage and telecommunications by -1.4 percentage points to 16.6%.

• ***The services sector had the greatest influence on the increase of gross added value***

In 2008, agriculture, fishing and forestry supported the seasonally adjusted growth in the gross added value (3.5%) by 0.4 of a percentage point, while their average contribution from the period from 2001 to 2007 was zero. Industry or the processing industry with an identical average contribution at the amount of 2.1 percentage points only contributed 1.6 percentage points and 1.2 percentage points respectively to the growth in the gross added value in 2008. The contribution of construction even fell into negative figures at -0.3 of a percentage point, while its average contribution in the medium-term horizon was 0.1 of a percentage point. Services as a whole contributed to the growth in the gross added value by 1.8 percentage points, but for all that they did not reach their average amount of 2.4 percentage points.



**Graph no. 2.1.12 The contributions of selected branches to the growth in the gross added value**  
(in percentage points, constant prices 2000, seasonally adjusted)



Source: the Czech Statistical Office

### Sources of economic growth

- **Intensive sources contributed more to the growth in GDP in total**

Whereas 2007 was marked by the above-average contributions of all these sources, in 2008 the medium-term average for the period from 2001 to 2007 was only exceeded in the case of the contribution of employment. The lower value of economic growth also meant the relative reduction of all its contributions. From 2004, the contributions to the growth in GDP gradually increased in total in the case of extensive sources, but in 2008 they fell to less than half (1.5 percentage points.) in comparison with the previous year. Even though the contributions of the intensive factors from 2006 also fell to 1.7 percentage points in 2008, they constituted more than half of the economic growth in total in that year.

- **The contribution from employment was higher than the average ...**

The gradual reduction of economic activities during the course of 2008 was reflected in the worsening conditions in the labour market and in the reduction of the growth rate for employment. Despite that, there was positive year-on-year growth and employment<sup>5</sup>, expressed in individuals, increased by 1.2% in 2008 year-on-year and it was therefore 0.4 of a percentage point higher than the medium-term average for the period from 2001 to 2007. The contribution has been on the increase since 2004 and in 2008 it contributed to the growth in GDP by 0.7 of a percentage point, whereby the average contribution in the period from 2001 to 2007 amounted to 0.5 percentage points.

- **... despite that, work productivity supported GDP growth the most**

In the previous four years, there has been a continuous reduction in the growth rate for work productivity to less than half its original value – in 2008, work productivity increased by only 2.0%. This growth was lower than the medium-term average of 3.7%. For this reason, work productivity also supported economic growth in a more limited manner at the amount of 1.0 percentage point, although the average contribution in the period from 2001 to 2007 reached 1.9 percentage points.

- **The contribution of capital reserves was the second highest of all the sources in 2008**

The capital reserve (the reserve of gross fixed tangible and intangible assets<sup>6</sup>) increased between 2001 and 2007 on average by 2% year-on-year. According to the preliminary estimate of the Czech Statistical Office, the growth in the capital reserve was in the area of this value despite the slowdown in the growth rate for gross fixed capital formation. The contribution of the capital reserve to the growth in GDP is also associated with this development. The contribution in 2008 reached the value of 0.8 of a percentage point and it thus corresponded to the medium-term average for the period from 2001 to 2007.

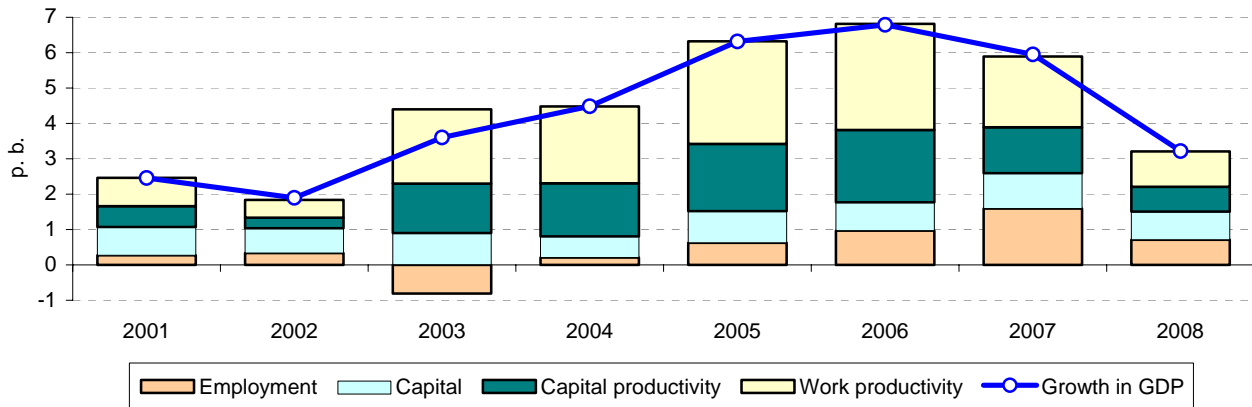
<sup>5</sup> The information on employment was taken from the national accounts for the reason of mutual comparability with the data on the gross domestic product and the reserve of gross fixed assets.

<sup>6</sup> The information on the reserve of gross fixed assets was available up to 2007: for this reason, its value for 2008 has been estimated.

- **The substantially below-average contribution of capital productivity**

It is possible to note growth of 1.2% in the capital productivity indicator (the reserves of gross fixed assets) in 2008; in comparison with the average for the period from 2001 to 2007 (2.4%), this involves a significant reduction in the growth rate. The average contribution of the capital productivity reached 1.3 percentage points, but the contribution in 2008 only amounted to 0.7 percentage points. Together with employment, capital productivity thus contributed identically and the least to the growth in GDP in the given year.

**Graph 2.1.13 The contributions of the production factors and their productivity to the growth in GDP (percentage points, constant prices 2000)**



Source: the Czech Statistical Office