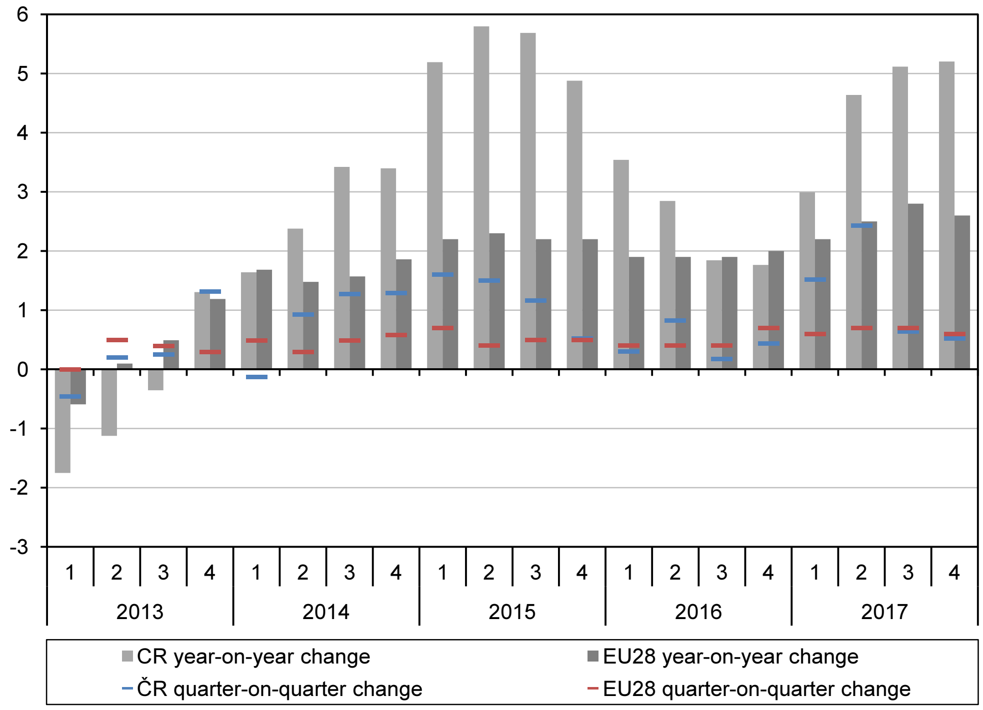
2. Overall Economic Performance

Year-on-year dynamics of the gross domestic product was exceeding 5% in H2.

The gross domestic product (GDP) expanded by 4.5%[1] in 2017. It represents the second highest value since the expansion year 2007. The economic growth was higher only in 2015, when the economy was considerably stimulated by the finalisation of drawing of resources from the European funds. The year-on-year dynamics was strengthening in the course of the last year. Acceleration manifested in comparison to year 2016 already in H1 (3.0% in Q1, 4.6% in Q2). The year-on-year growth was 5.1% in Q3 and 5.2% in Q4. All GDP components shared in the high year-on-year increase. The growth was supported in a stable manner by the large contribution of the domestic consumption (especially households) as well as the foreign demand over the whole year. On these foundations, a growing contribution of the investment activity could have built in the second half of the year. The quarter-on-quarter dynamics differed from the year-on-year one. The GDP attained the highest quarter-on-quarter additions in Q1 and 2 (1.5% and 2.4%), the pace slackened to 0.6% and 0.5% in individual quarters in the second half of the year. The gross value added (GVA) increased by 4.5% in 2017. The year-on-year growth of GVA somewhat exceeded the GDP addition in Q4 itself, when it reached 5.4%.

Chart 1 **GDP** (volume indices, adjusted for seasonal and calendar effects, in %)



Source: CZSO, Eurostat

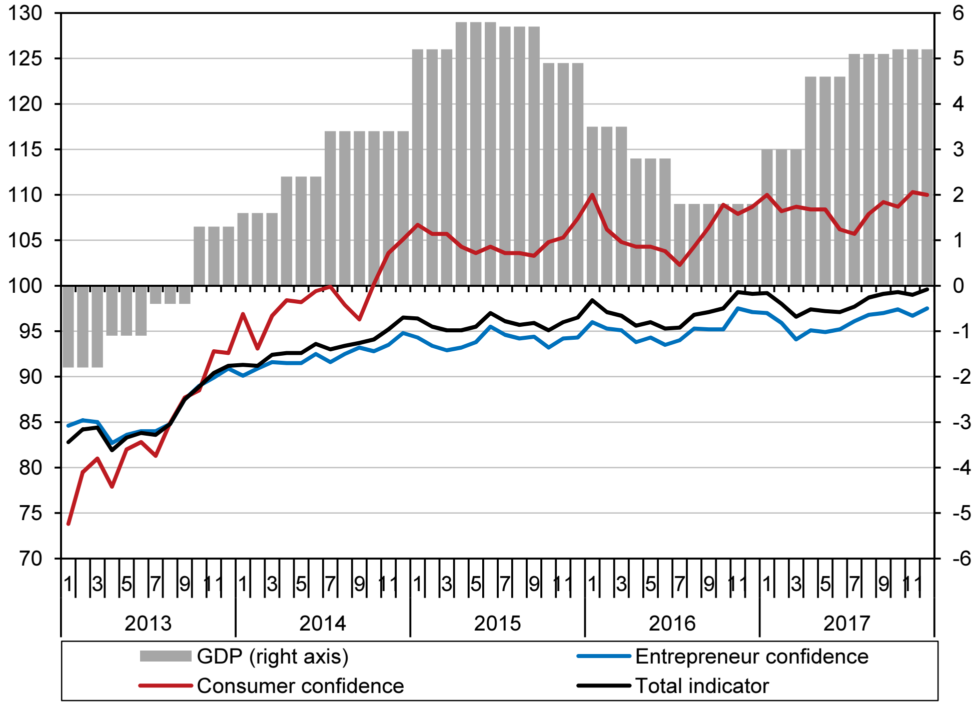
The European economy also prospered.

The year-on-year GDP growth gained pace compared to year 2016 in the European Union as well. The GDP expanded by 2.4%[2] in the EU last year. It moderated to 2.6% year-on-year in Q4 itself. Romania achieved the highest GDP increase based on the available data in 2017, specifically 7.0%. Malta (6.6%) and Slovenia (5.0%) were other strongly growing economies. According to data for Q1 to Q3, Ireland will likely be placed on the position of the fastest growing economy or tightly below, where the year-on-year dynamics was manifesting even double-digit values. Economies of Italy (1.5%, still the highest growth since 2010), Belgium (1.7%), Great Britain (1.7%) and France (1.8%) had to face less than 2% growth. Countries neighbouring the Czech Republic also enjoyed a successful year, which was in the end favourably mirrored in the performance of the domestic economy via foreign

[1] The development of the GDP, gross value added and their components is expressed with the help of the volume indices (i.e. adjusted for changes in prices) and adjusted for seasonal and calendar effects. Data were published on 2. 3. 2018 and the revised data will be published on 3. 4. 2018.
[2] Data for Ireland and Luxembourg not available. Slovakian data are not adjusted for calendar effects.

trade. German economy increased pace and its GDP rose by 2.2% in 2017 here, Slovakia strengthened by 3.4%, Poland experienced a jump acceleration to 4.6% and Austria also nearly doubled its growth (2.9%) compared to year 2016. Quarter-on-quarter dynamics of the GDP growth in the EU crossed the 0.5% boundary in 2017 (0.6%, 0.7%, 0.7% and 0.6% in individual quarters).

Chart 2 **GDP** (volume indices, adjusted for seasonal and calendar effects, year-on-year in %, right axis) **and confidence indicators** (2005=100, left axis)



Source: CZSO

Domestic consumption expanded fastest since year 2007. Mostly households were spending.

Domestic consumption expenditures grew by 3.3% in 2017, which is the most since 2003. Year-on-year growth of the household consumption accelerated (4.0%, the most since 2007), on the contrary the government expenditures were not expanding as fast as in the preceding two years last year (1.6%). The dynamics of the household consumption reflected the marked growth of wages as well as the positive expectations regarding the future economic development. Its year-on-year growth overtook the 4% boundary in Q2 to Q4. Similarly to GDP, the quarter-on-quarter dynamics of consumption also slowed down during the year. The quarter-on-quarter additions of expenditures on total consumption amounted to 0.6% in both Q3 and 4. The household consumption itself also increased in the same way during Q4. Look on the year-on-year dynamics of expenditures based on durability showed, that the growth of expenditures on durable items slowed down the most in 2017 (from more than 10.0% to 5.9%[3]) and the growth of expenditures on short term consumption goods (4.1%) and services (2.7%) accelerated. Total consumption expenditures contributed to the year-on-year GDP growth by 1.7 p.p.[4] in 2017, in that household consumption by 1.4 p.p. Consumption contributed to growth the most in Q2 (1.8 p.p.). The contribution was shrinking moderately in the next time periods. As is evident from the comparison of additions to the GDP development after and without exclusion of imports for final use, the accelerated growth of the household consumption was to a considerable extent saturated by foreign supply in Q2 to Q4.

Growth of household consumption was partially satiated through foreign supply.

Wages and salaries markedly grew in both nominal and real terms.

The mentioned growth of wages was really exceptional. Nominal increase of the volume of paid out salaries and wages achieved 7.9% in 2017, the most since year 2007. Rising inflation led to the increase in the difference between the real and

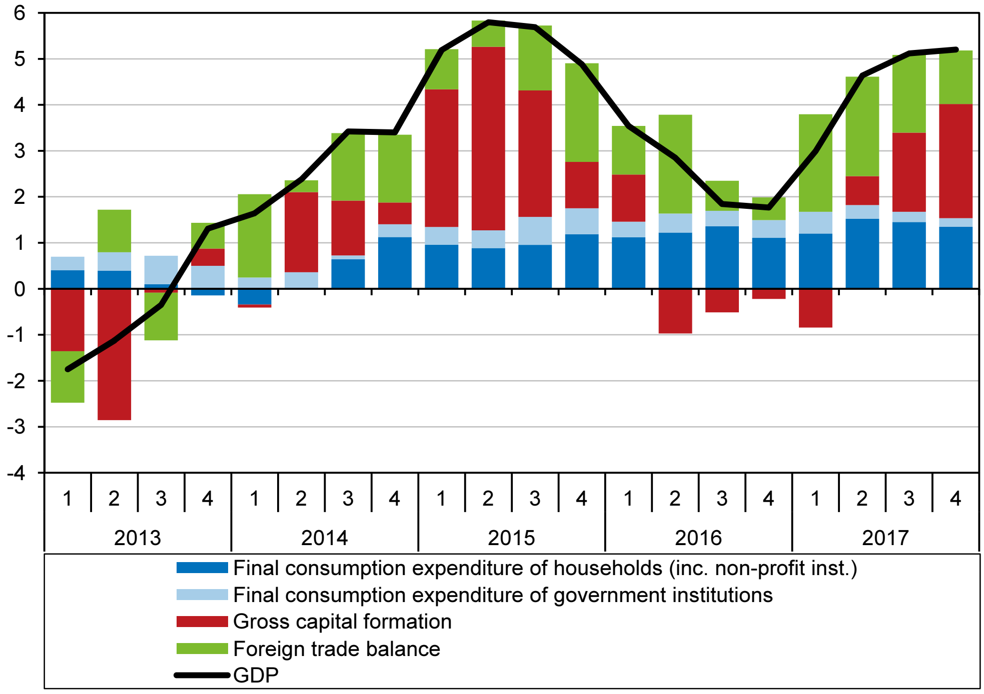
[3] Data regarding the household consumption based on the durability of goods are not seasonally adjusted.
[4] Contributions to GDP change after exclusion of imports for final use.

nominal growth of salaries and wages compared to years 2013–2016. In real terms, there was by 5.3%[5] of paid out wage resources more last year. The pace of the volume of paid out salaries and wages was accelerating during the year and it reached 8.4% in Q4 (the most since Q2 2008). Growth of total employment (persons) also mildly increased last year and arrived at 1.6%[6]. Total employment gauged by the number of hours worked grew faster (1.9%).

Wages grew in all branches. It was accompanied by growth of total employment as well.

Manufacturing, which employs the highest number of workers, drove the total growth of wages and salaries in the last year. The volume of paid out wage resources increased by 8.6% here, while the employment did not increase much in this branch (0.6%). Trade, transportation, accommodation and restaurants is on the second place, the volume of wages rose by 8.3%. At the same time the employment increased here by 2.4%. Salaries and wages in the branches with the predominance of the public sector rose by 8.5%. Information and communication achieved the highest growth of the volume of earnings (9.1% given the 3.8% growth of employment). Professional, scientific, technical and administrative activities experienced the same growth of employment, but lower volume of the paid-out wages (7.9%). Construction (3.6%) and financial and insurance activities (4.5%, the only branch with the reduction of employment of 1.0%) attained the lowest growth of the paid-out wages.

Chart 3 **Contributions of expenditure items to real GDP change***
(volume indices, year-on-year growth, contributions in p.p., GDP in %)



* Contributions to GDP change after exclusion of imports for final use. Source: CZSO

Investment supported the acceleration of the year-on-year GDP growth in H2.

Investment activity stood behind the strong GDP growth in Q3 and 4. Contribution of the expenditures on gross fixed capital formation to the GDP growth amounted to 1.2 p.p. in 2017. The importance of the investment activity for the GDP growth was increasing during the year. As with the consumption expenditure the increased demand for investment goods was also partially saturated by the foreign supply. Investment rose by 5.8% in 2017. Although this GDP component was still stagnating in Q1. In the following three quarters, the year-on-year additions already exceeded 7.0% and the investment expenditure rose by 7.9% in Q4. In part the low comparative basis from year 2016 had an effect, nevertheless the quarter-on-quarter dynamics showed the increase of the investment activity especially in Q2 and 3. Based on the type classification of gross fixed capital formation, investment into the

[5] Converted into the real expression using the deflator of final consumption expenditure of households.
[6] In the national accounts conception, seasonally adjusted.

Look on the type classification of the gross fixed capital formation implies, that mostly businesses and households invested.

transport vehicles and machinery (8.9%[7]), housing (7.0%) and ICT and other machinery and equipment (6.6%) grew the fastest in 2017. First two mentioned categories experienced a moderation of the year-on-year rate of growth, the third and most significant by volume item offset the fall from year 2016. Stated composition of the expenditure on gross fixed capital formation points to the key role of businesses and households in the last year investment activity. The growth of investment into the products of intellectual property also increased (to 5.4%). On the contrary, expenditures on other buildings and structures remained on the exceptionally low level of year 2016 last year, when their growth attained 0.9%. This investment category includes infrastructure projects, which are the domain of the government institutions sector. At the same time, it also consists of various industrial buildings and warehouses. Both strong economic growth and the logistically advantageous location of the Czech Republic stimulated their construction.

Foreign trade surplus mildly grew last year. Trade with services is mostly behind it.

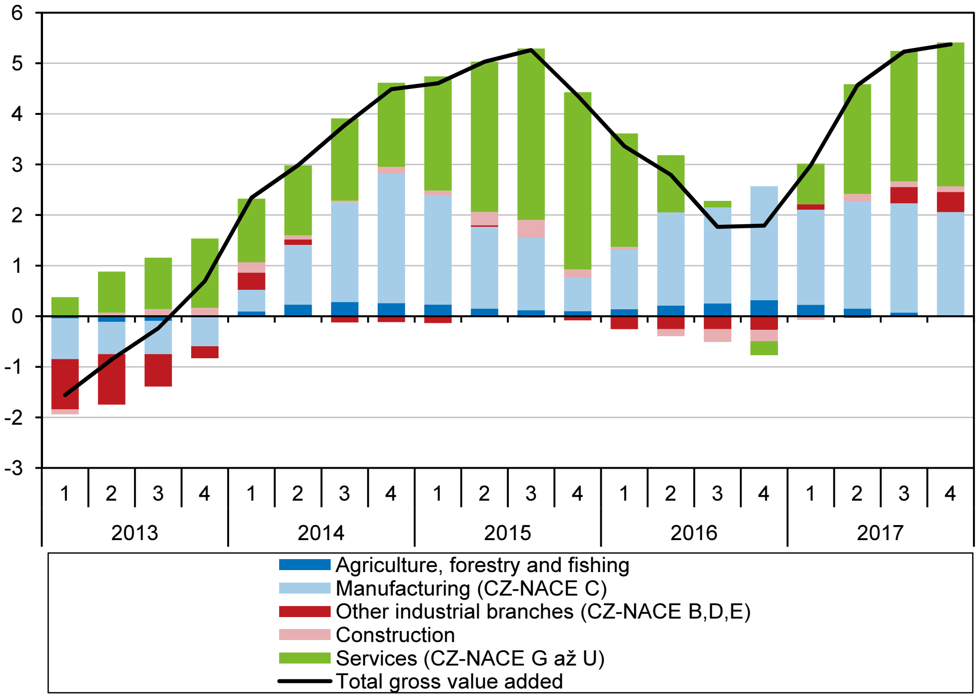
Foreign trade resulted in positive balance in the amount of 364.5 CZK bn[8] in 2017 and thus the increase of 8.0 bn manifested. The growth of the surplus could be observed in all quarters, its main part however was created in Q1 (year-on-year increase of 6.5 CZK bn.). Total increase is the result of a marked enlargement of the surplus of the trade with services balance (122.3 CZK bn, year-on-year addition of 13.0 bn). Surplus of the foreign trade with goods arrived at 242.3 CZK bn last year and it shrank by 5.0 bn year-on-year. The terms of trade were 99.0% in year 2017. They moderated during the year and already reached a positive result in Q4 (100.3%). Loss from the movements of the terms of trade, expressed as a difference between the GDP and the real gross domestic income in 2017, arrived at 38.5 CZK bn. It presented the first negative result since year 2012.

Manufacturing and services sector both supported to the same extent the year-on-year growth of GVA.

View of the supply side of the GDP confirms the continuing key role of manufacturing in the Czech economy. The gross value added of the relevant branches increased by 7.6%. The addition to the total year-on-year growth of the GVA was very stable throughout the year and it was 2.1 p.p. The services activities were also very important. Total contribution of services to the GVA growth achieved also 2.1 p.p. last year and the role of services was strengthening during the year. Their addition to the year-on-year growth of GVA was 2.8 p.p. in Q4. Among the services branches, the trade, transportation, accommodation and restaurants contributed the most (0.6 p.p.) together with the professional, scientific, technical and administrative activities (0.5 p.p.). Finance and insurance activities also fared well (contribution 0.4 p.p.). All branches contributed positively in the last year, so even construction, which experienced relatively adverse situation in 2016 also achieved a positive, even though a small contribution in the last year (0.1 p.p.).

[7] Data regarding the type classification of gross fixed capital formation are not seasonally adjusted.
[8] Based on the methodology of the national accounts.

Chart 4 **Contributions of branches to real change in GVA** (volume indices, year-on-year contributions in p.p., GVA in %)



Source: CZSO