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First half of 2020

Summary Data on the Czech Republic

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Latest information provided in this report has been dated the 7th September 2020.

Aggregated data for the EU used in this text contain all 27 Union states except for Great Britain.

1. Summary

- The Czech economy experienced the deepest downturn in Q2 2020 in its history. Gross domestic product (GDP) decreased by 11.0% in real terms year-on-year[1] and by 8.7% quarter-on-quarter. Lowering of the foreign trade with goods and services balance surplus mainly contributed to the very deep economic slump. This was linked to the suspension of operations in some domestic as well as foreign businesses. Apart from the halt of export, demand on the part of buyers abroad also decreased. Expenditure on gross capital formation also had an adverse effect on the GDP growth. The investment activity itself fell by 4.8% in Q2 year-on-year. The domestic consumption, especially the household consumption, which decreased by 7.6% year-on-year also shared in the GDP decrease. The economic downturn was also very substantial in the European Union. Year-on-year decline amounted to 13.9%, the GDP fell by 11.4% quarter-on-quarter.
- Gross value added (GVA) plunged by 10.9% year-on-year and by 9.4% quarter-on-quarter. Given the broad impact of the measures, the GVA fell in majority of branches. The year-on-year slump was very strong in manufacturing. Especially the manufacturing of motor vehicles as well as its associated branches were hit hard. Activity in some branches of services was often directly restricted, which was mostly apparent in the grouping trade, transportation, accommodation and food service (GVA decreased by 20.5%). Despite universal decline, information and communication managed to maintain mild year-on-year rise (1.1%). GVA decrease did not spare construction (–6.2%).
- The value of export of goods slumped by 215.1 CZK bn year-on-year in Q2. Value of imported goods fell by 169.5 CZK bn (19.0%). Resulting balance achieved surplus of 11.4 CZK bn, it however worsened by 45.6 bn year-on-year. Sale of motor vehicles, which was the main reason of the surplus growth in the recent years, affected the worsened balance the most. The balance worsened by 49.6 CZK bn in Q2 here. The usual deficit of trade with oil and natural gas on the contrary eased by 19.8 CZK bn in connection with the slump of their prices.
- Year-on-year dynamics of the consumer prices reached 3.1% in Q2 and slowed down slightly compared to Q1. Food and non-alcoholic beverages, whose year-on-year additions accelerated to 6.5% contributed the most to the growth of the consumer prices. In contrast, the growth of prices of housing and energies slowed down to 3.2% in Q2. Impact of increased consumption tax only took full effect in Q2 and the prices of alcoholic beverages and tobacco were raised by 6.6%. Prices of accommodation and food service also kept notable dynamics (5.1%). While prices of food service rose by 5.5%, addition to prices of accommodation slowed sharply down in Q2 (2.5%). Only prices of transportation reduced the total growth of consumer prices (–3.4%).
- Setting of basic monetary policy-relevant rates changed downwards during Q2. Rates on client deposits also reacted relatively fast to this development, especially rates on deposits with agreed maturity. Interest rates on credit for households as well as businesses were also cut. However, in the uncertain economic environment, both households and businesses were more restrained in utilising credit financing.
- The measures associated with pandemic manifested on the labour market mainly as the downturn of economic activity in Q2. Total employment dropped by 1.4%[2] quarter-on-quarter and it was decreasing especially in manufacturing and in part of services. General unemployment rate however went up only slightly (it was 2.7% in June), among other things due to large share of persons, who left the labour market in the crisis (foreigners, working seniors). The average wage grew only by 0.5% year-on-year in Q2. The development was also considerably diversified. The average wage fell the most in the strongly hit branch of accommodation, food service and restaurants, wages were nevertheless falling also in other services. Wages also plunged in manufacturing. In contrast, the average wage rose in information, communication and in energy as well as in services with predominance of the public sector. Given the strong growth of consumer prices however, the average wage in the economy fell by 2.5% in real terms.
- State budget shortfall reached 195.2 CZK bn in H1. Impacts of the pandemic measures were apparent on both revenue and cost side of the budget especially in Q2. Total revenues dropped by 5.9% year-on-year in H1. On

[1] Data regarding the GDP, gross value added and their components are expressed in constant prices and adjusted for seasonal and calendar effects.

[2] Employment data are in the national accounts conception adjusted for seasonal effects.

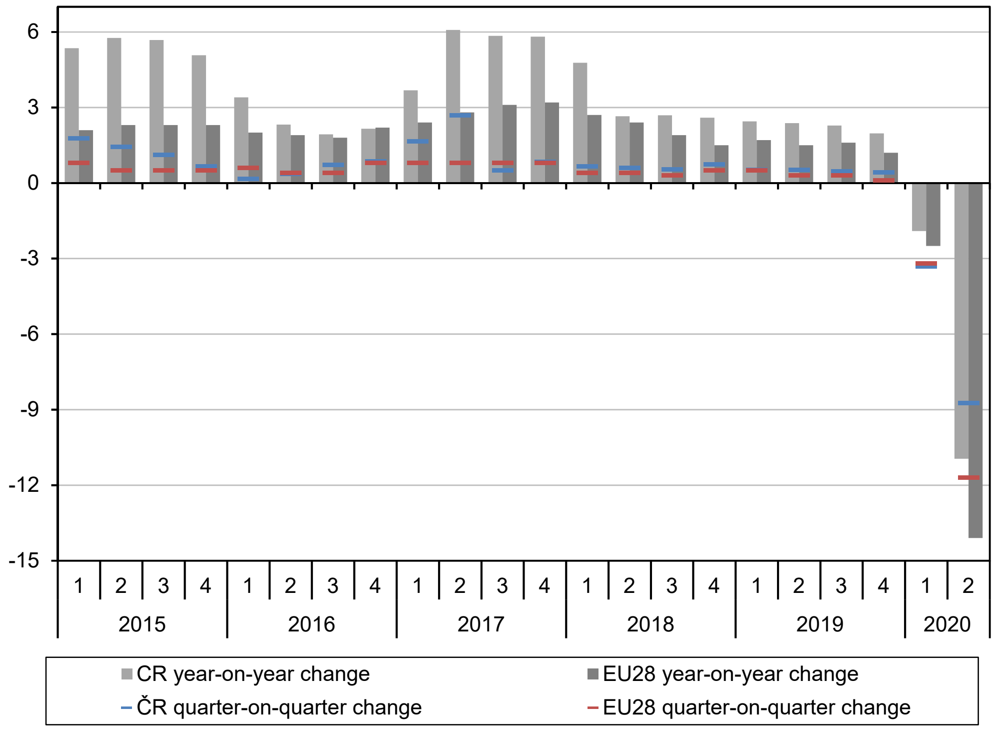
the revenue side, the main occurrence was the evaporation of tax collections resulting from the hampered economic activity as well as measures to strengthen the liquidity of businesses affected by downswing in sales. Costs on the contrary increased by 17.0%. More than one third of current expenditures increase was connected to the counter pandemic measures, higher drawing on social benefits however also contributed by similar rate.

2. Overall Economic Performance

In relation to covid-19, the Czech economy recorded the deepest downturn in its history.

The Czech economy underwent the worst economic downturn in its history in Q2 2020. The Gross domestic product (GDP) sunk by 11.0%[3] year-on-year (the previous deepest fall from Q2 2009 was 5.4%). It was the consequence of the extraordinary situation of the counter pandemic measures, when the operations in large part of the economy, especially services, retail trade as well as some important industrial branches were halted or restricted. The development commencing already during March, affecting also the results of Q1 (GDP decrease of 1.9%) thus continued. All its components exerted influence upon the GDP in the direction of its downturn in Q2. The strongest was the slump of foreign trade balance (–7.9 p.p.)[4]. It was partly caused by the suspension of production in some domestic export-oriented businesses, partly also by the decrease of demand on the part of foreign producers employing domestic suppliers. Domestic consumption and investment however went also down. In comparison to Q1, the GDP declined by 8.7% and it also represented the deepest recorded fall (previous largest decrease was 3.4% and occurred in Q1 2009). Compared to Q1, the quarter-on-quarter downturn deepened for all GDP components.

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



Source: CZSO, Eurostat

The whole EU experienced deep economic downturn.

Year-on-year decline of GDP attained 13.9%[5] in the European Union in Q2. In accordance to expectations, it represented the worst recorded result in history. Since practically the whole Union was tackling more or less strict restrictions related to the coronavirus for the most part of the quarter. View of the individual GDP components shows a sharp decline of both consumption and investment activity. Disturbance of the foreign trade and subsequent balance worsening however also had large effect. The GDP fell by 11.4% in the Union compared to Q1. While several economies managed to maintain year-on-year growth still in Q1, the downturn already struck all EU countries

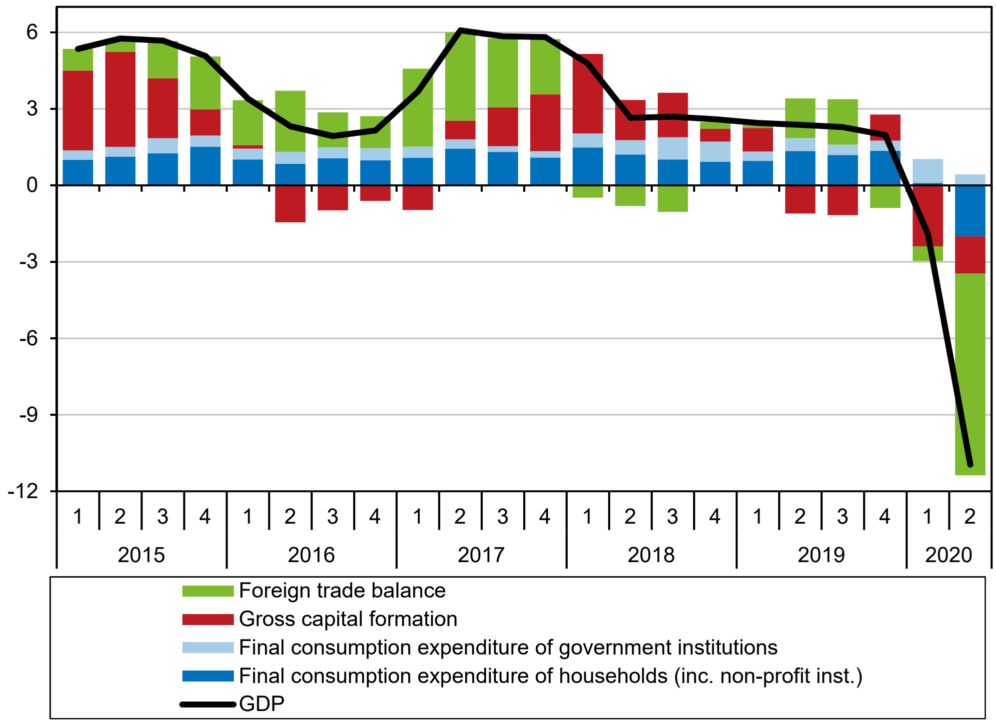
[3] The development of the GDP, gross value added and their components is expressed with the help of the volume indices (i.e. adjusted for changes in prices) and adjusted for seasonal and calendar effects. Data are valid as of 1st September 2020.
[4] Additions to the GDP change after exclusion of imports for final use.
[5] Data for Luxembourg not available. Data for Slovakia not adjusted for calendar effects.

according to the available data in Q2. The largest year-on-year decline occurred in Spain (–22.1%), France (–18.9%) and Italy (–17.7%). The GDP decrease was the most moderate in Ireland (–3.7%), Lithuania (–4.0%) and in Finland (–6.3%).

Turning point was apparent in the development of both employment and wage dynamics on the labour market in Q2.

The economic downturn also hit the volume of paid out wages and salaries, which went down by 5.3% year-on-year in Q2. It presented the first fall since the end of year 2013. At the same time, the notable price growth continued in the economy, which impinged upon the development of the household purchasing power. Real decrease amounted to 8.3%[6]. Reversal occurred also in the development of total employment (expressed in persons), whose year-on-year decrease accelerated to 1.9%[7]. The total employment reduced by 1.4% compared to Q1. The fall of the number of hours worked was even more pronounced (year-on-year –10.7%, quarter-on-quarter –7.8%). Volume of paid out wage resources was shrinking the most in manufacturing year-on-year (–11.5%, drop of employment was 3.5% here). Similarly, deep downswing also occurred in grouping trade, transportation, accommodation and restaurants (–11.2%, employment decreased by 3.2%). In case of professional, scientific, technical and administrative activities, the volume of salaries and wages reduced by 9.7% in Q2 and total employment dropped by 4.4%. Other branches of services nevertheless maintained the year-on-year growth of wages, even if weaker compared to Q1. Real estate activities experienced an increase of 6.4%, financial and insurance activities 5.8%, information and communication 4.7% and activities with predominant government sector[8] 4.1%. Following more than three-year period, fall of paid out wages eventuated also in construction (–2.8%) and agriculture, forestry and fishing (–2.3%).

Chart 2 Contribution of expenditure items to real GDP change* (volume indices, year-on-year growth, contributions in p.p., GDP in %)



Source: CZSO
*after exclusion of import for final use

[6] Converted into the real expression using the deflator of final consumption expenditure of households.
[7] Employment in the national accounts conception (persons), figure seasonally adjusted.
[8] Public administration, education, health and social work.

Household consumption diminished. Government institutions heightened their expenditure year-on-year.

Total year-on-year fall of domestic consumption reached 4.8% and its contribution in the direction of GDP fall was 1.6 p.p. Consumption reduced year-on-year for the first time since Q4 2012. Household consumption was exclusively falling, households had limited options, where and what to spend, given the introduced measures. Year-on-year decrease of household consumption thus arrived at 7.6% and it concerned the deepest recorded slump. Government institution consumption on the contrary went up by 1.8% year-on-year. Quarter-on-quarter decrease of the total consumption was 4.8%. Deep slump related to households (–6.3%), government consumption however also decreased (–1.5%). Development of consumption with respect to durability[9] completely reflected the situation in the economy. Expenditure on items of short-term consumption fall was relatively moderate year-on-year – by 1.7%. Closure of large part of shops with non-essential goods then besides other things led to large fallouts of consumption of long-term consumption goods (–12.2%) and medium-term consumption goods (-25.0%). Consumption of services plunged by 13.8% in Q2.

Investment activity plunged year-on-year, but mildly increased quarter-on-quarter.

Expenditures on gross capital formation dropped by 10.2% year-on-year in Q2 and contributed 1.5 p.p. to the total GDP decrease. In that expenditures on gross fixed capital formation decreased by 4.8% year-on-year. Inventory stock exerted a negative influence. Quarter-on-quarter development painted a more optimistic picture regarding the investment activity. While the expenditures on gross capital went down by 8.5% compared to Q1, investment activity (gross fixed capital) increased by 0.9%. Analysis of the type classification of gross fixed capital formation revealed, that other buildings and structures were the only investment category, where the expenditures went up year-on-year (6.7%)[10]. Other categories on the other hand recorded decrease. Investment into the transport equipment (–19.5%) and ICT and other machinery and equipment (–12.3%) shrank the most. Moderate year-on-year decrease then affected the products of intellectual property (–1.3%) and housing (–0.3%). From the type classification of investment, it can be indirectly assumed, that the investment activity of government institution sector (other building and structures) was the least disrupted. In contrast, the non-financial businesses were, given the situation, likely more restrained in the area of investment (machinery, transport equipment).

Foreign trade was hardly hit by the crisis. Trade balance with both goods and services experienced record worsening.

Both export and import of goods and services markedly decreased in real terms in Q2. Year-on-year slump of export reached 23.3%, for import it was 18.2%. Although the balance of foreign trade with goods and services[11] thus attained a surplus of 44.1 CZK bn, it presented the worst result for 2nd quarter since year 2012. Positive balance diminished by 56.5 CZK bn year-on-year. Significantly negative impact of the balance development on the year-on-year growth of GDP was also heightened in comparison to the exceptionally successful Q2 2019 (surplus reached 100.6 bn). Mainly the surplus of trade with goods dropped (22.0 CZK bn, decrease by 47.9 bn), but the positive balance of trade with services was also falling (22.2 bn, decrease by 8.5 bn). The services balance last overtook the goods in Q3 2011.

Measures were directly aimed at part of services, which impinged upon the drastic decrease of their GVA.

Gross value added (GVA) descended by 10.9% year-on-year in Q2. The decrease at the same time affected the majority of branches. In comparison to the preceding quarter, the GVA dropped by 9.4%. Majority of both services and industry branches were afflicted. The fall of GVA was especially strong in the grouping trade, transportation, accommodation and restaurants (–20.5%, contribution to the total GVA decrease was 3.8 p.p.). It concerned activities, which were directly impacted by the restrictions aiming at slowing down spreading of the infection. Manufacturing was also markedly hit (–18.2%, effect on the total GDP growth –4.6 p.p.). Here, the production

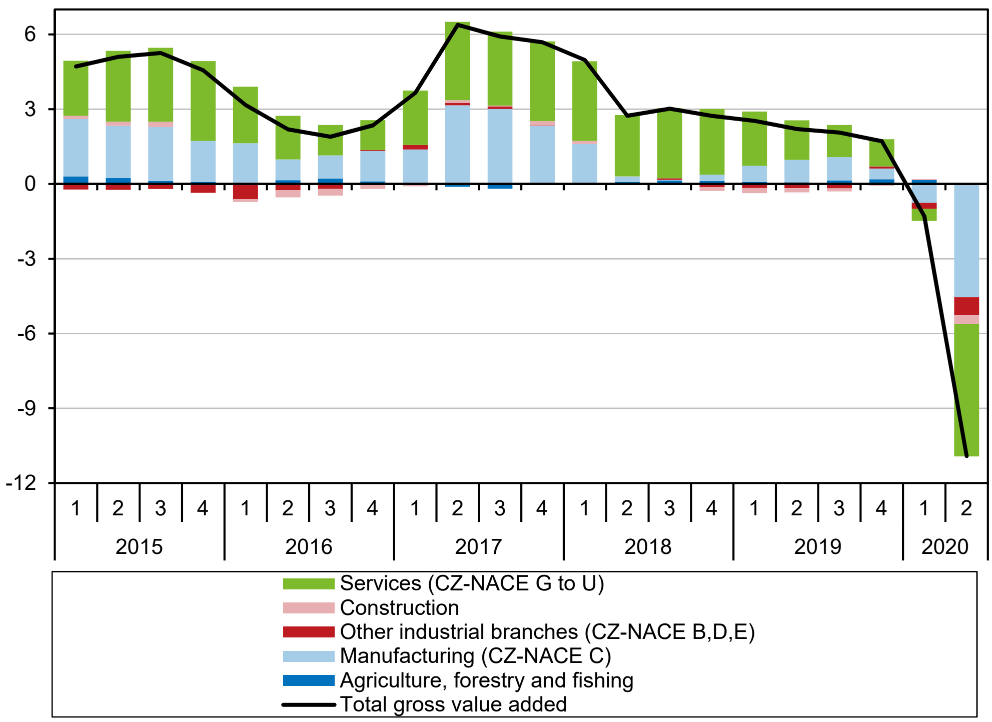
[9] Data regarding consumption based on durability are in domestic conception and not seasonally adjusted.
[10] Data regarding the type classification of gross fixed capital formation are not seasonally adjusted.
[11] According to the methodology of quarterly national accounts (export and import in FOB/FOB prices).

was restricted by the decision of the producers themselves, partially due to the easier abiding by the epidemiologic measures, limited demand on part of both domestic and foreign buyers however also played a role.

GVA grew in information and communication year-on-year.

Decrease of GVA in other branches was more result of both social and economic operations being brought to a standstill. Lowering of the GVA in professional, scientific and technical activities was 6.4% and it was the first since Q3 2011 (effect on GVA decrease –0.5 p.p.). The gross value added in financial and insurance activities went down by 5.1% year-on-year in Q2. Real estate activities recorded the fourth decrease in a row (–3.1%). Despite the total situation, information and communication on the contrary maintained the year-on-year GVA growth (1.1%) and partially thus assessed its indispensable role. The GVA markedly fell in construction (–6.2%), whose part was facing a lack of labour force, mainly the foreign labour force. By contrast, the GVA grew in agriculture, forestry and fishing (1.0%).

Chart 3 Contributions of branches to real change in GVA (volume indices, year-on-year contributions in p.p., GVA in %)



Source: CZSO

3. Branches Performance

Quarter-on-quarter decrease of GVA deepened down to 9.4% in the whole economy in Q2.

If the restrictive pandemic measures severely hit primarily the branches closely tied to tourism in Q1 2020, it already managed to paralyse a large part of the economy during the subsequent quarter. The gross value added (GVA)[12] thus dived by record 9.4% quarter-on-quarter and markedly deepened its descend from Q1 (–2.4%). In year-on-year expression, the GVA decreased by 6.1% in the whole H1 and slightly overtook the intensity of similar downturn from the first half of the crisis year 2009. Half-yearly performance of the Czech Republic ranked more to the average among the EU states (to the 12th place out of 23 states with available data[13]). Mainly the countries of the southern wing of the euro area registered the deepest downturn (for instance Spain 12.9%, Italy 11.8%, Portugal 8.7%) and also France (12.1%). By contrast, mainly the northern states and also the majority of newer EU members (with accession after year 2000) have so far enjoyed a relatively favourable position, for example Lithuania (–0.8%), Bulgaria (–2.7%), Poland (–3.5%). Differences between the states primarily reflect the outbreak of the coronavirus infection across the EU, speed and intensity of the government measures and partially also the varying branch structure of economies (larger proportion of branches tied to tourism had an adverse effect, the role of public services or agriculture then a positive effect).

The highest year-on-year economic performance downturn afflicted mainly the states of the euro area southern wing in H1. The CR belonged to the average.

Manufacturing dragged the economic performance down the most.

Year-on-year decline of the value added in the domestic economy was from nearly one half the result of considerable slump of manufacturing in H1 2020 (contribution 2.7 p.p., decline of the branch itself by 10.6%). This branch simultaneously due to the influence of its weight dragged down the whole economy the most both in Q1 and Q2 of this year. Non-manufacturing industrial branches also recorded weaker performance by more than one tenth in H1. The effect of several weeks' disruption of production stemming from the sanitary measures, but also lowered demand were evident here as well[14]. Construction was progressing substantially better, the impacts of the onset of economic recession were not apparent at the beginning there. Its performance even slightly improved thanks to the large stock of orders as well as favourable weather in Q1. The GVA already decreased in Q2 (by 6.2%). The already demanding administrative process of structures preparation became complicated further due to the declared state of emergency, number of projects was suspended. The branch was limited by the lack of labour force, many workers returned only slowly after reopening of the borders to the CR. This factor was also valid for branches of the primary sector, which manifested in the reduction of the hours worked (by more than 5% in H1). Despite this development, the GVA grew here already third year in a row (+4.1%, the most out of 11 main branches). It was thanks to the stabilised situation in the agriculture primary production, which was not negatively affected by the regulatory influences except for stricter sanitary measures. Meat production stagnated in H1; the domestic producers sold naturally by 5% milk more. The continuing natural wood industry also supported the growth of the whole primary sector.

The negative impacts started to manifest with a slight lag in construction.

Both animal production and forestry assisted the output growth in the primary sector.

Value added was decreasing the most in branch trade, transportation, accommodation and restaurants.

The segment trade, transportation, accommodation and restaurants also experienced strong macroeconomic impact (contribution –2.2 p.p.). The GVA sank by one eighth among other things due to the radical restriction of the international movement of people[15] here – that is the most among the main branches. The influence of other branches of the tertiary sphere was of a lower order. Still, some of them were hit strongly – especially so-called other services[16], where the GVA dropped by one tenth (in that by more than one fifth in Q2).

[12] Data regarding the GVA are expressed in constant prices and adjusted for seasonal and calendar effects.
[13] Fresh data regarding the GVA for H1 were not available for Ireland, Luxembourg, Croatia and Romania.
[14] Planned technological shutdowns of production facilities stood behind the decrease of output in energetics (coincidentally also especially during March and April 2020).
[15] Final consumption expenditures of non-residents in the CR decreased by more than one third year-on-year, in Q2 2020 itself even by unprecedented 62%. Non-residents share in the total household final consumption expenditures in the CR in the long-term roughly 6%.
[16] Include cultural, amusement and recreation activities or personal services for household (among other hairdressing, cleaning services or repairs of products and equipment).

Pandemic measures strengthened the role of public services and information and communication.

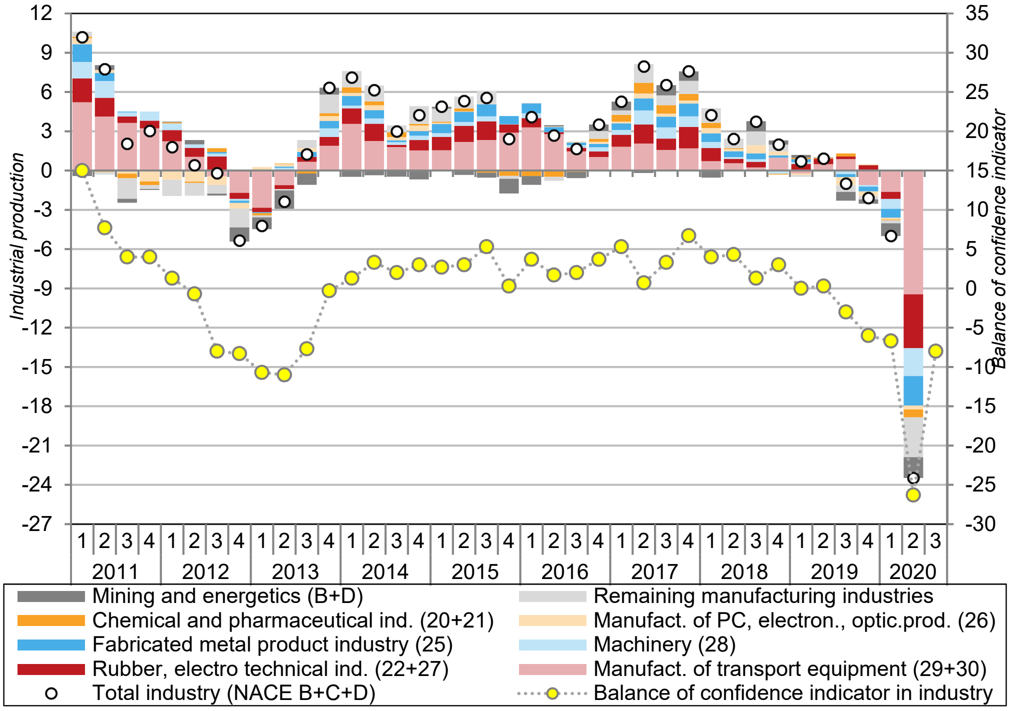
Smaller decrease in the size of 2 to 3% was similarly apparent in professional, scientific and technical activities, further then in financial or real estate activities. On the contrary, the GVA stagnated in public services[17] ensuring the basic operations of society. The role of information and communication also gained in relevance in the pandemic time period. Still the value added increased in this dynamic branch the least in the last eight years (+1.3%).

March and April freeze of activity of key export businesses led to record slump of industrial production.

More detailed data from the business statistics also prove an unparalleled strong and fast impact of counter pandemic measures on the output of domestic industry. If the industrial production[18] fell quarter-on-quarter „only“ by 3.7% in the first quarter of this year, second quarter saw deepening to yet unseen 18.3%. The record this year´s downturn was fundamentally affected by the development at the turn of both quarters – the production lowered by more than one tenth in March, by nearly one quarter in April. The measures against spreading of the coronavirus gradually led to the disruption or complete breaking of supply chains. Number of businesses started to limit production during the second half of March, many practically suspended it (it concerned especially the key companies of the motor vehicle industry and their domestic subcontractors). Many suspended branches recovered relatively fast in the subsequent months, regardless of this however this year´s July output in the whole industry still slightly lagged behind the "pre-pandemic" (February) level (by 4%).

July production still slightly lagged behind the pre-pandemic period.

Chart 4 Contributions of sub-branches to the year-on-year change of the industrial production (in percentage points, adjusted for calendar effects), **balance of confidence indicator in industry*** (in p.p., right axis)



*Balance of confidence is seasonally adjusted and expresses the situation in the first month of the given quarter.
Source: CZSO

More than one half of year-on-year industry fall was attributed to manufacturing of motor vehicles and their

Industrial production slumped by 23.6% year-on-year in Q2 2020. Apart from the pandemic supply shock the effect of the previous cyclical industry slowdown also accumulated (interconnected with the former decrease in the euro area), already apparent for the most part of the last year[19]. The downturn amounted to 14.4% for the

[17] Contain public administration, education, health and social work.
[18] Includes branches of mining and quarrying, manufacturing and also energetics (here as activities of production and distribution of electricity, gas, heat and air conditioning supply). All year-on-year rates of growth of output (at the level of branch sections as well as divisions) are adjusted for calendar effects, both quarter-on-quarter and month-on-month rates then also for seasonal effects.
[19] Shallow quarter-on-quarter decrease of industrial production in the CR occurred already in Q3 and Q4 2019 (–1.6% and –0.6%). Since it was accompanied by the reduction of employment, the domestic industry fell into technical recession at the end of last year.

closest subcontractors in H1.

whole H1. Manufacture of motor vehicles participated in it by more than one third, together with the immediate associated branches (electrical equipment, manufacture of rubber and plastic products) then by more than one half. Consequently, both machinery and metalworking industry contributed similarly by approximately one tenth.

Industrial production fell by more than one fifth in the motor vehicle, mining as well as leather manufacturing in H1. Slump of machinery was also significant.

Not surprisingly, the deepest downturn affected manufacturing of motor vehicles in H1 (–27.8 % year-on-year), since the utilisation of production capacities was only 50% at the beginning of Q2. The output in coal mining and leather manufacturing also dived approximately by one quarter, it however depicted a long-term trend. The fall of the machinery output by more than 17% was much more substantial, which mirrored the significant decrease of private investment in the whole economy.[20] The weight significant manufacture of metal products, metallurgy, but also for example manufacturing of beverages decreased their output by one seventh. In contrast, the food industry achieved only mild decrease (–2.4%), since the volume of household expenditure on items of short-term consumption was by the restrictive measures affected only marginally in H1 (–0.5%). The relatively diversified branch other manufacturing was in a similar situation supported by growing demand for medical supplies. This was partially also linked to the higher output of the pharmaceutical industry (+4.9%), where the growth of output is however a longer-term phenomenon. Wood and paper industry were also mildly growing branches this year, here it is likely the consequence of the increasing natural wood logging in the recent years. The three growing branches above however assisted the growth of the total industrial production only by 0.2 p.p. in H1.

The specific structure of demand on the contrary aided some especially smaller fields during the coronavirus crisis.

Sales from industrial activities strengthened year-on-year only in energetics, pharmaceutical and food industries.

Nominal sales of businesses from industrial activity recorded similar development as the industrial production this year. Following mild year-on-year decrease in Q1 (–3.1%) they plunged in the subsequent quarter (–23.8%). Only companies in energetics (+6%), pharmaceutical industry (+6%) and food industry (+2%) earned more for the whole H1. Price growth partially aided in offsetting the decrease of real production to manufacturers of wearing apparel and leathers, in contrast the mild growth of output was not a guarantee of sales strengthening in wood and paper industry. Larger plunge of prices in the chemical industry or metallurgy adversely affected the sales of businesses and further amplified the adverse development of output in these branches. Total sales of industrial businesses from direct export declined by 15% compared to H1 of the last year, domestic sales only by 10%. Faster pace of domestic sales compared to foreign in essence endured also in the period 2017 to 2019.

Domestic sales still kept showing higher pace than sales from direct export.

Decrease of new orders moderated in the summer period. Utilisation of production capacities still did not reach the pre pandemics level.

Short term industry outlook still remained unfavourable in the summer period. The value of industrial orders[21] was by more than one quarter lower in Q2 2020 (without substantial differences in rates of growth between domestic and foreign demand). Only small branches signalled low growth – pharmacy and also the manufacturing of other (mainly rail) transport equipment, where the development is traditionally strongly volatile. Orders in the manufacture of motor vehicles were lower by 44%, which can be understood as a sequel of the April suspension of production. July data brought more favourable indications, when the orders grew by one tenth (in the manufacture of motor vehicles), resp. moderated the fall to 4% (in the whole industry). Still below average utilisation of production capacities (both in the whole industry and motor vehicle segment) proved, that the situation in industry was still far from stabilized after the spring shock. The large share of businesses considering the inadequate demand as a growth barrier was also unfavourable[22] (63% at the beginning of Q3, the most in the last seven years). Only 15% weight of the lack of workers signals considerable cooling of the labour market (the least since the end of year 2015). At the

Inadequate demand troubled nearly two thirds of industrial businesses.

[20] In 2009 even more significant downturn occurred, when the volume of fixed investment fell by 9.2% year-on-year and machinery output slumped by 28%.

[21] Surveying of orders is ongoing only in selected CZ-NACE sections (13, 14, 17, 20, 21, 24, 25, 26, 27, 28, 29, 30), which manufacture mostly custom-made products, with longer production cycle and larger stocks of orders.

[22] Businesses could have stated more main barriers simultaneously. All data from business cycle surveys are seasonally adjusted.

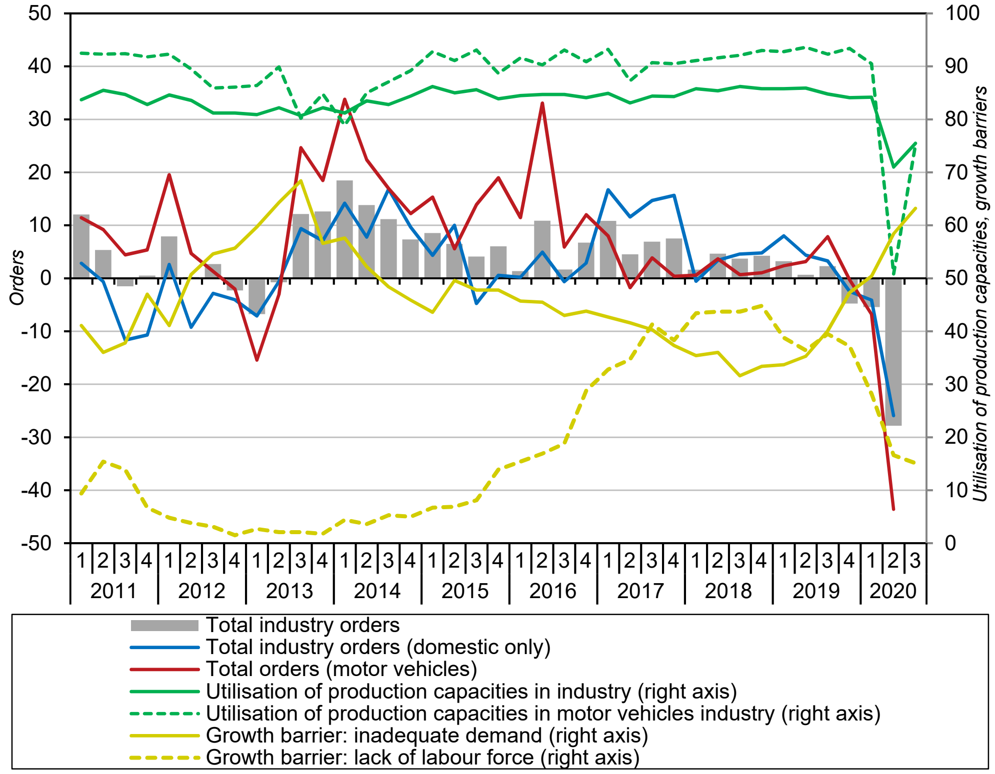
Markedly negative balance of confidence persisted in machinery.

same time the expectations of businesses in the area of employment remained negative (at the level of recession – 2012). Balance of entrepreneur confidence indicator in industry improved during the summer, it ended on –6 points in August and thus reached the level from the beginning of this year. Among the individual branches, the largest pessimism persisted in machinery (–31 points), manufacture of furniture (–27) and manufacture of wearing apparel (–26). The sentiment was more favourable in the manufacture of motor vehicles and achieved the same value as at the end of last year (–2 points).

Year-on-year slump of industrial production in the CR was the eighth largest among the EU states in H1.

While the industrial output in the EU went down by similar pace as in the CR in H1 year-on-year (–5.3%), the Union decrease was milder in Q2 (–19.2%). Luxembourg and Italy registered the biggest downturn in the whole H1 (similarly –18%) in the whole H1, followed by strongly industrial economies of Slovakia (–18%) and Romania (–17%). Decrease in the CR was the eight highest within the Union (–14%), Hungary or Germany also recorded a similar pace. Poland, where the distinct structure of industry also had an effect (for example higher proportion of branches linked to agriculture), fared better (–7%). Output of industry increased only in Ireland (+3%) – due to higher share of high-tech branches – and also in Malta (+2%). In the CR (–20.0%) similarly to the whole EU (–18.5%), the production shrank the most in branches manufacturing products of investment nature (e.g. machines, transport equipment).

Chart 5 New orders in manufacture of motor vehicles, in industry in total (in current prices, year-on-year change in %) **and utilisation of production capacities in industry*** (in %, right axis) **and selected barriers to growth*** (in %, right axis)



*Both utilisation of production capacities and growth barriers are seasonally adjusted and express the level in the first month of the given quarter.
Source: CZSO

Following the favourable development at the beginning of the year, construction experienced downturn in

Construction entered the year 2020 resolutely. Large stock of public, but also private orders together with very favourable weather were reflected in the continuing growth of the construction output[23]. It increased by 1.1% quarter-on-quarter in Q1. This branch however started to gradually face difficulties in the subsequent period. The introduced

[23] All year-on-year data regarding the construction output are adjusted for calendar effects, quarter-on-quarter as well as month-on-month rates of growth then also for seasonality effect.

Q2. The downturn was evident primarily in the building construction and affected rather small and medium businesses.

government restriction measures hindered the administrative process of construction preparation, various competitive tenders were interrupted, which disrupted the continuity of construction. It also further deepened the already pressing difficulty with the availability of labour force in construction. Construction output thus slumped by 7.0% quarter-on-quarter, which represented a stronger shock than a short-term fallout of public infrastructure investment at the beginning of year 2016 (due to the transition to the new EU programme period). The construction output decreased year-on-year by nearly 9% in Q2. More than three years lasting growth period thus ceased. In contrast to year 2016, when the whole branch was dragged down by the civil engineering construction, the building construction had a negative impact this year. Mostly small and medium businesses were struck by the fallout here, it can be assumed that these companies had at their disposal less sufficient reservoir of orders from the recent expansion period. In contrast the output of civil engineering construction grew also thanks to the accelerating stage of drawing on the EU funds in both this year´s quarters (+15.5 resp. +1.7%).

Several years lasting growth of commenced as well as completed flats halted this year.

Volume of residential construction mildly shrank in H1 2020. Completed flats recorded faster decrease, their number (15.3 thousand) decreased by 7% year-on-year. Less flats were built in new residential buildings (–1.1 thousand), number of flats in non-residential buildings or family houses went on the contrary slightly up. Number of all commenced flats lowered only negligibly (by 2.4%), again mostly due to lower construction of residential buildings. By contrast the number of flats in family houses has been expanding for already the sixth year, when it exceeded 10 thousand and its size was already approaching the highest half yearly totals from the expansion period 2006 to 2008.

Approximate value per one building permit stagnated, new orders slightly increased in Q2.

The approximate value per one building permit remained nearly the same (–0.6%) for the first seven months of year 2020 in comparison to the last year´s value. Low growth of both residential (+4.6%) and non-residential buildings (+3.9%) was compensated by deeper decrease for civil engineering structures (–9.1%, partially due to high last year´s basis). The approximate average value per one building permit amounted to 4.6 CZK mil in the same period and stagnated year-on-year. Favourable fact was, that the value of newly concluded domestic orders (in firms with 50 and more employees) slightly increased in Q2 (by 6.9% year-on-year), thanks to both building and civil engineering construction. The total stock of work in the form of not yet realised construction orders was also strengthening. It was by one tenth higher year-on-year at the end of Q2, due to both public and private orders[24]. The peripheral segment of foreign orders also strengthened after more than five years. More than three fifths of stock of work still belonged to domestic public orders.

Entrepreneur confidence descended to 2.5 years minimum in construction. The main growth barrier of the branch slowly shifts from lack of human resources to lack of work contracts.

Balance of entrepreneur confidence indicator in construction worsened since the beginning of this year and dropped to 2.5 years minimum (–16 points) at the beginning of summer. 38% of construction firms considered the inadequate demand a significant barrier to growth, the same proportion then also the lack of employees in August 2020. The two-year period, when construction was primarily limited by labour force likely ended. The trend of growing inadequate demand is apparent since the beginning of this year.

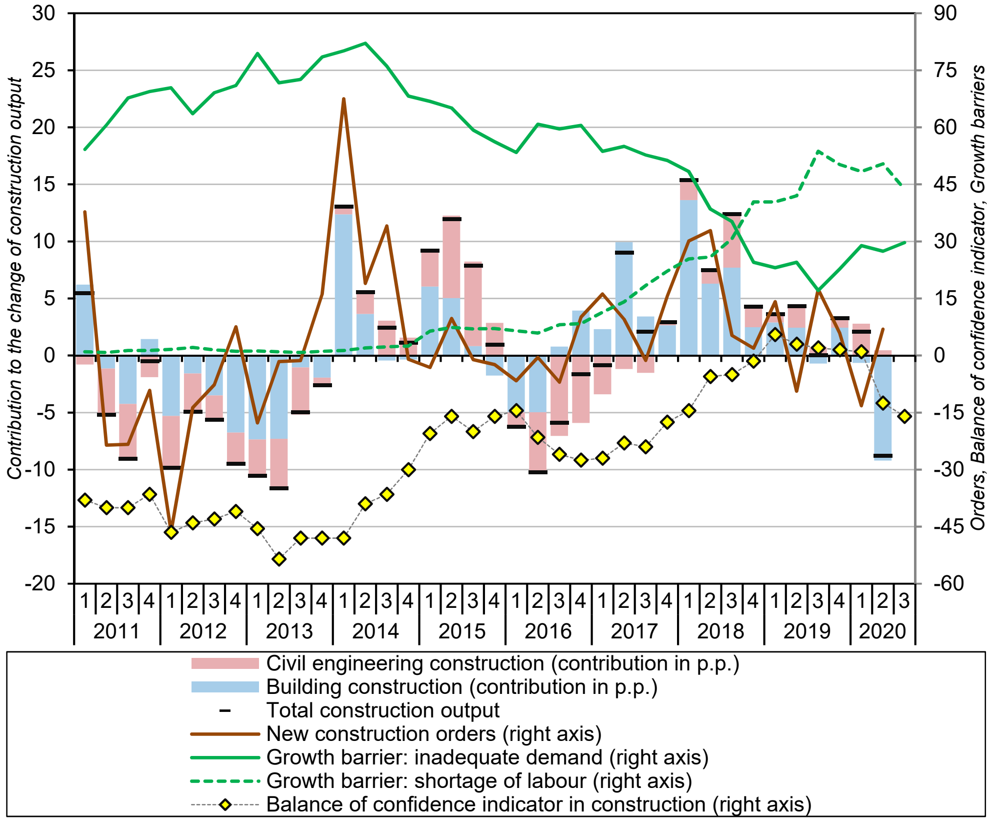
Construction output fell in the CR less than in the EU, especially thanks to the improved output of civil engineering construction.

Construction output decreased by 7.8% in the EU in H1 – that is by nearly doubled pace compared to the CR. The largest fall from the monitored countries[25] affected France (–23.5%) and Spain (–16.0%). This contrasted with nearly 20% growth in Romania. Increase occurred in further eight countries, among others in Germany (+3.6%) and in Poland (+0.1%). All newer member states from central and eastern

[24] Construction firms that have work ensured on average for the ten months ahead.
[25] Greece, Italy and Cyprus were not assessed for the reason of absence of current figures.

Europe attained better result than the EU, in many places also contributed by the swift growth of the civil engineering construction.

Chart 6 Contributions of branches to year-on-year change of construction output (in p.p.)**, new construction orders** (year-on-year in %, right axis)**, balance of confidence indicator in construction*** (in p.p., right axis) **and selected barriers to growth*** (in %, right axis)



Data Related to construction output are adjusted for calendar effects.
*Balance of confidence and growth barriers are seasonally adjusted and express the situation in the first month of the given quarter.
Source: CZSO

Sales in services dived approximately by one tenth month-on-month in March as well as April.

Sales in selected services[26] were considerably hit by the restrictive measures of the government. They fell by 8.9% month-on-month already in March 2020. They nearly halved in the sub-branches associated with tourism, since these businesses were practically able to operate only in the first half of the month. The decrease of total sales mildly deepened in April (–10.4%). Gradual revival in the subsequent months in reaction to loosened restrictions took place very slowly. Quarter-on-quarter decrease thus reached deep 14.4% in Q2, which was double the so far record downturn from the beginning of year 2009.

Mainly weaker output in transporting and storage, and also downturn in accommodation, food service and restaurants stood behind the decline of sales in services.

Sales in services decreased by 12.0% year-on-year in H1 2020. It was mainly result of development in transporting and storage (contribution – 4.5 p.p.) and branch accommodation, food service and restaurants (–3.0 p.p.). Other branch sections were however hit as well – information and communication then the least (contribution +0.3 p.p., branch growth 1.7%). While some divisions of this branch benefited from the heightened demand during the corona crisis (telecommunication activities, ICT areas), others were affected to a varying degree (publishing activities, programme production and broadcasting activities and especially so called motion picture and musical industry, where the sales

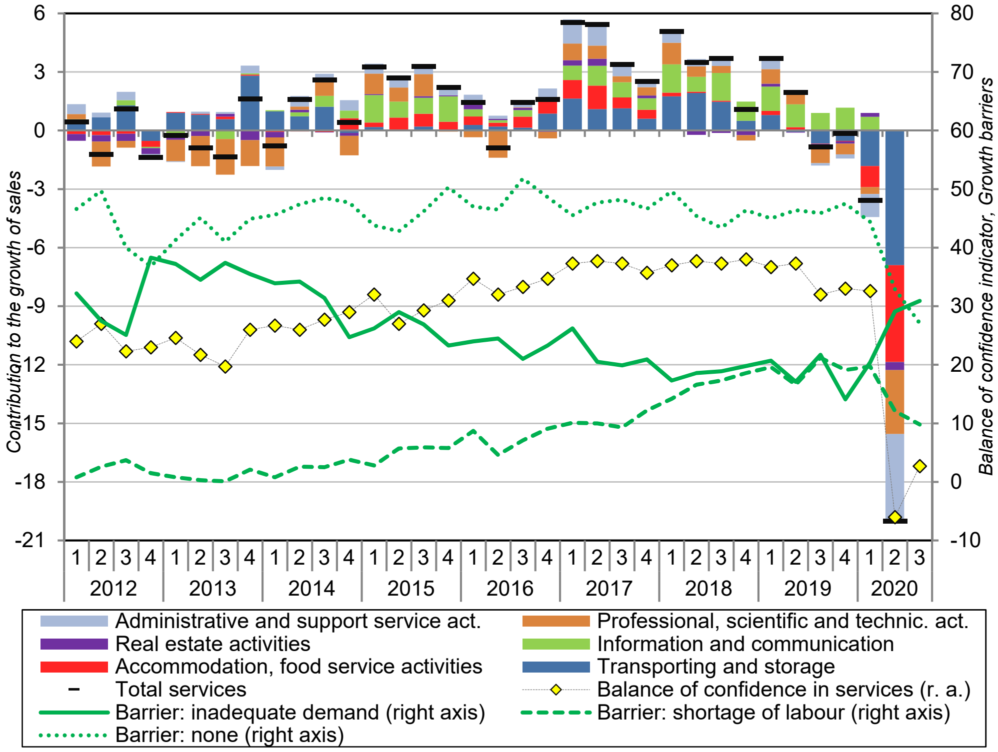
[26] Without branches trade, financial activities, insurance activities, science, research and public services. All data for services are in constant prices, year-on-year data are adjusted for calendar effects, quarter-on-quarter and month-on-month data are adjusted for seasonal effects (including the number of working days).

Only telecommunications, ICT areas and postal and courier services continued to grow.

dropped by more than one third[27]). The branch transporting and storage also featured diverse development. Deep drop of the air transport (–63.9%) as well as significant decline in key division of land and pipe transport (–15.0%) contrasted with the growing demand for postal and courier services (+8.8%). The sales fell by nearly two fifths in accommodation, food service and restaurants. In accommodation itself, the slump reached 53.4%[28]. Branch administrative and support service activities recorded nearly one quarter plunge of sales. Expected deep decrease of performance of travel agencies emerged (–63.9%), sales of job agencies also lowered by nearly one quarter. Drop of nearly one tenth also affected the branch professional, scientific and technical activities. Mainly lower output of other processional and scientific activities had an adverse effect (–13.0%) and also both architectural and engineering activities (–8.1%), demand was however falling in all sub-branches, including long-term growing market research and public opinion polling. Legal and accounting activities remained affected the least. Moderate decline was also registered in the real estate activities (–1.3%).

Four years lasting rise of sales for market research and public opinion polling halted.

Chart 7 Contributions of branches to year-on-year change of sales in services* (in p.p., adjusted for calendar effects), **balance of confidence indicator in services**** (in p.p., right axis) **and selected growth barriers**** (in %, right axis)



* Without branches trade, financial activities, insurance activities, science, research and public services.
**Includes also the financial sector. Balance of confidence and growth barriers are seasonally adjusted and express the situation in the first month of the given quarter.
Source: CZSO

Retail sales growth stopped due to the impact of both restrictions

Retail sales[29] fell by 2.3% during Q1 2020 (it was the first quarter-on-quarter decrease since the end of year 2013). Similar rate of growth was also repeated in the subsequent

[27] According to the Union of motion picture distributors, the sales from entrance fees in the cinemas in the CR decreased by 56% year-on-year in H1 2020. It was consequence of several weeks' interruption of the cinemas operations and later also the limited offer of motion pictures. The number of visitors was lower nearly by one half - to 709 thousand year-on-year even in July (lower July figure was last recorded in 2000).
[28] The number of overnight stays of non-residents in mass accommodation facilities decreased by 54% in the CR this year compared to H1 2019, for non-resident tourists even by 64%. The fallout was for the most part blanket, both from the view of the type of facility and the region of accommodation. Even after easing most of the barriers connected to the across the border movement of persons, the arrival tourism in the CR remained to a large extent paralyzed. The year-on-year decrease of all overnight stays was 60% in June, in that 90% for foreign visitors.
[29] All year-on-year rates of growth of retail sales are stated in constant prices and adjusted for calendar effects (including the number of working days). Retail includes branches CZ-NACE 47.

and deteriorated consumer confidence. End of Q2 however saw a mild boost.

period. These results were fundamentally affected by the pandemic measures, which limited the purchasing ability of the population, especially in March and April[30]. The whole industry faced still weakened demand on the part of non-residents even later and purchasing appetite of domestic households was inhibited by the worsening consumer confidence, sharp lowering of nominal average wages as well as growing concerns of households regarding potentially rising both prices and unemployment. Despite this development, a still delicate growth of sales year-on-year renewed in both May (+0.7%) and July (+1.9%).

Retail decline was driven especially by significant reduction of sales for fuels in H1.

Retail sales declined by 1.7% year-on-year for H1 2020. Sales for fuels contributed the most to this decline. These decreased by nearly one eight and recorded first drop in the half-yearly accumulation since the end of year 2013. Even though a considerable lowering of fuels consumer prices occurred in Q2, marked dive of the freight transport as well as weaker regular commuting to work (as a consequence of spreading work from home) proved to be a more important factor. Sales of non-food products fell only slightly (by 0.3%). Development in individual specialised shops however differed. While the sales of wearing apparel, footwear and leather goods or cultural and recreation goods registered double digit fall, demand for computer as well as communication equipment, pharmaceutical, health and cosmetic products or household goods slightly grew. Strengthening growth of sales via internet or mail order was however pivotal (+28.4%, in that by +37.8% in Q2). Sales for food dropped by 0.3% in H1. The mild decrease was particularly affected by weaker sales in specialised shops (–13.6%). Dramatic downturn, its depth exceeding the slump from year 2009, afflicted the motoring segment sales this year (–22.6%).

Growth dynamics of sales via internet was further gaining strength.

Retail sales fell by doubled pace in the EU compared to the CR in H1.

Retail sales fell by 3.5% year-on-year in the EU in H1, that is by more than double the pace in the CR. Sales dived by more than one tenth in Italy, Spain and Bulgaria, they fell strongly also for instance in Slovenia (by 9.5%). On the contrary growth was observed in ten states, the highest in Finland (+3.7%), further in Germany (+1.9%) and the Netherlands (+1.7%). Weak growth was recorded also for example in Poland or Hungary.

[30] Retail sales slumped by 10.5% month-on-month in March, by further 1.8% in April. Sales already grew in the subsequent three months and they returned to the pre-pandemic level in July.

4. External Relations

Value of export plunged in Q2.

Total value of export of goods attained 1 625.7 CZK bn in H1. Export sank by 253.8 CZK bn year-on-year (13.5%). It represents the largest decrease in this time period since year 2009 (–198.1 bn, 16.6%). In Q2 itself, the value of export was 733.0 CZK bn and it decreased by 215.1 bn year-on-year (22.7%). Comparison with Q2 2019 deepened the decrease even further – from the view of the value of export, it was the most successful recorded quarter. The development was definitely influenced by the restrictions on the social as well as economic operations in reactions to spreading of the coronavirus. Beginning of the measures can be dated to half of March (year-on-year slump of export by 11.5%), when also some large export companies restricted or temporarily closed their operations. Especially April and May were fully hit (year-on-year decreases by 38.1% and 29.0%), in June the export already mildly increased (0.3%).

The downturn involved nearly all important export destinations.

Export slump was all encompassing and touched nearly all main export destinations. Export into the EU sank by 210.5 CZK bn (14.0%) in H1 and it arrived at 42.6 bn (11.4%) outside the EU. Majority of stated decrease however belonged to Q2 (export into the EU –176.0 CZK bn, outside the EU –38.5 bn). In Q2, export to Germany (–65.1 CZK bn, –21.9%), France (–18.1 bn, –37.2%) and Slovakia (–15.8 bn, –18.7%) went down the most. Exporters to Spain (–14.8 bn, –43.9%), Poland (–13.4 bn, –22.8%) and Italy (–10.0 bn, –27.6%) also recorded strong decreases. In case of countries outside the Union, especially the slump of value of export to Great Britain (–11.8 CZK bn, –33.5%) is noticeable. Here, a series of decreases lasts with some exceptions already since Q3 2016 and the last decrease only deepened the existing trend[31].

Sale of motor vehicles was hit the most.

In Q2 export fell the most for items, which are vital for the Czech economy, and manufacturing of motor vehicles was the most affected branch. Value of export of motor vehicles decreased by 117.0 CZK bn (43.6%) year-on-year in Q2. The second strongest decrease was related to machinery and equipment (–23.1 CZK bn, –21.9%). Export was also falling in branches tied to manufacturing of motor vehicles – electrical equipment (–14.8 CZK bn, –19.1%) and rubber and plastic products (–12.0 bn, –23.8%). Further strong decreases were recorded for metal products (–10.3 bn, –17.4%), basic metals (–8.1 bn, -21.8%), chemicals and chemical products (–7.1 bn, –16.1%).

Import also slumped. Apart from the restricted economic activity the effect of decreased prices of oil and natural gas was also apparent.

Value of import of goods also fell in H1, specifically by 200.4 CZK bn (–11.3%) to 1 574.0 bn. In that a slump of 169.5 CZK bn (–19.0%) occurred in Q2. The resulting value of import was 721.6 bn. The import from the EU was falling more significantly (–143.5 CZK bn – 24.6%) than from countries outside the EU (–24.2 bn, –8.0%) in Q2. Import from Germany (-64.7 bn, –28.1%), further Russia (–15.7 bn, –57.0%, value decrease was also strengthened by the year-on-year plunge of prices of oil and natural gas) and Poland (–16.7 bn, –21.8%) dropped the most. Substantial increase of import from China (20.9 CZK bn, 24.2%) contributed to more favourable results of import from countries outside the EU. It is the largest addition since year 2010.

The value of trade with motor vehicles was also falling the most on the import side.

Development of both import and export was with respect to its type structure similar in many features. Value of import of motor vehicles slumped the most in Q2 (–67.4 CZK bn, –45.4%). Very strong decreases were further observed for machinery and equipment (–20.7 CZK bn, –22.8%), oil and natural gas (–20.8 bn, –63.0%, mainly due to the plunge of prices) and basic metals (–19.5 bn, –28.0%). Already several quarters lasting fall of the value of import of chemical substances and products further deepened to 13.8 CZK bn (–19.2%). The largest increase of import value since Q3 2018 on the contrary occurred for computers, electronic and optical products (15.0 CZK bn, 16.5%). Only March interrupted here the

[31] Share of export to Great Britain on the total value of export was 5.2% in Q2 2016. It was 3.2% in Q2 2020. The share was 4.2% for year 2019.

series of strong increases lasting since December 2019. The import of textiles also had exceptionally high addition (3.7 CZK bn, 27.6%). The import grew here the most in April and May.

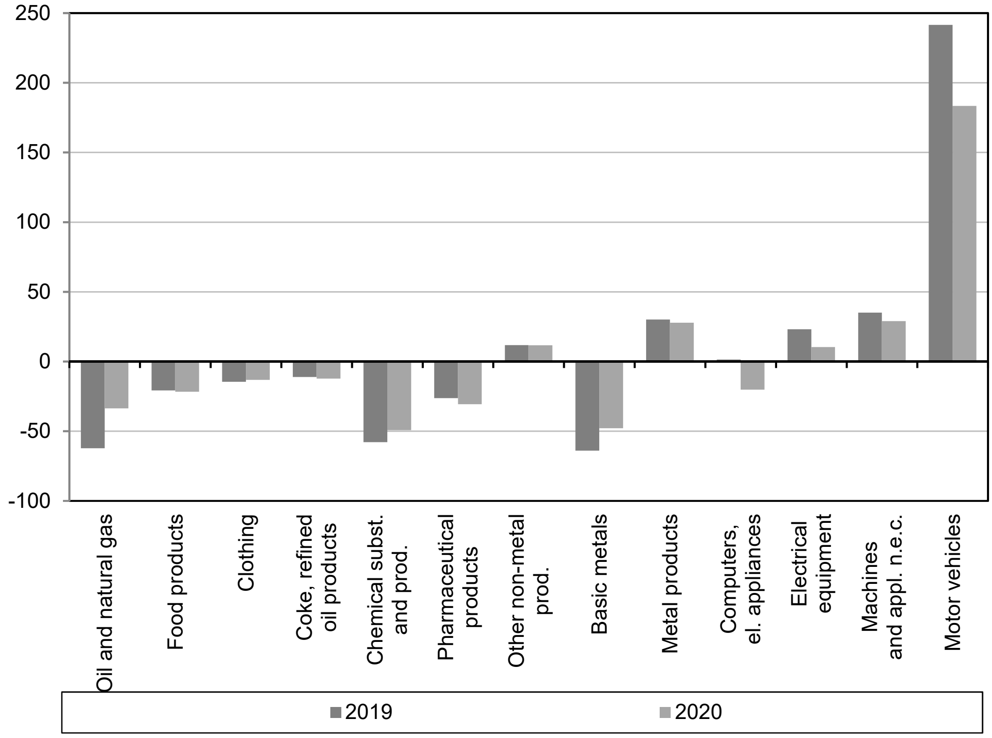
Foreign trade balance markedly worsened, especially for trade with the EU countries.

Large slump of export value over import also led to the worsening of balance of foreign trade with goods. It reached surplus of 51.7 CZK bn in H1. However, the positive balance reduced by more than one half in comparison to the same period of the previous year (53.5 CZK bn). Surplus arrived at 11.4 CZK bn in Q2 and decreased by 45.6 bn year-on-year. The trade with China (deficit deepening by 21.6 CZK bn), Spain (surplus decrease by 9.9 bn) and Great Britain (surplus worsening by 9.1 bn) affected the most worsening of balance in Q2. Lowering of positive trade balance with France (–8.7 CZK bn), Slovakia (–6.3 bn) and Hungary (–3.5 bn) was also significant. Year-on-year improvement of balance occurred for trade with Russia (+12.2 CZK bn, also thanks to the decrease of prices of oil and natural gas the balance ended uncharacteristically in surplus of 6.3 bn). Further trade with Poland (+3.3 CZK bn), Japan (+2.9 bn) and the Netherlands (+2.6 bn) worked in the direction of balance improvement.

Surplus of trade with motor vehicles recorded the largest slump.

Lowering of surplus of trade with motor vehicles contributed the most to the year-on-year worsening of balance in Q2 (–49.6 CZK bn), further deficit deepening for computers, electronic and optical products (–16.6 bn) and worsening of surplus for electrical equipment by 9.2 bn. Significant worsening of balance was also recorded for textiles (–4.8 bn), rubber and plastic products (–4.0 CZK bn), other transportation equipment (–2.5 CZK bn) and machinery and equipment (–2.4 bn). The influence of prices on the other hand stood behind the significant improvement of trade with oil and natural gas (+19.8 CZK bn) as well as basic metals (+11.4 bn). Deficit for chemical substances and products also moderated (+6.7 CZK bn).

Chart 9 Balance of foreign trade with goods in foreign trade statistics (accumulation first half year, in CZK bn, selected divisions of the CPA classification)



Source: CZSO

5. Prices

Year-on-year growth of the price level strengthened in Q2.

Year-on-year growth of the price level[32] accelerated to 4.2% in Q2. It presents the highest addition since Q1 2009. Compared to Q1, the year-on-year dynamics strengthened. Price level for consumption goods was raised by 3.3%, which is less than in Q1. Pace of consumption of goods by both households and the government sector slowed down. Prices of capital goods grew by 1.9% year-on-year in Q2 and thus the descent of the rate of growth apparent already in the previous quarter continued. Weakening of the price growth for domestic expenditure items was offset by notable increase of the terms of trade. They amounted to 102.1% in Q2, the most since Q4 2009. The terms of trade were positive for both trade with goods (102.1%) and services (101.8%).

Year-on-year growth of consumer prices mildly slowed down in Q2.

Total year-on-year increase of consumer prices rose by 3.4% in H1. The year-on-year dynamics of the consumer price index slightly slackened in Q2 and attained 3.1%. Especially the strong January month-on-month addition (1.5%) affected the year-on-year comparison the most. The month-on-month dynamics subsequently slowed down, but year-on-year additions remained above the 3% level. March as well as April saw a mild month-on-month decrease, but May and June brought an acceleration. Food and non-alcoholic beverages and further housing and energies pushed the year-on-year growth of prices the most in Q2. Contribution of alcoholic beverages and tobacco notably strengthened (their sharp month-on-month as well as year-on-year increase occurred in May and June). On the contrary, the prices of transportation had a downward effect.

Food and non-alcoholic beverages contributed to the growth the most.

Food and non-alcoholic beverages the most affected the growth of the total index in Q2. Year-on-year addition to their prices further accelerated to 6.5% compared to Q1. Price of majority of types of food were raised apart from oils and fats (–2.8%). Prices of fruit achieved the highest increase (25.8%), where the pace gained speed. Addition to prices of meat (10.8%) and also other food products (10.5%) remained very strong. Prices of vegetables (6.5%), sugar, jam, honey, chocolate and sweets (5.4%) also hiked up. The year-on-year dynamics of prices of baking products and cereals (3.2%) as well as milk, cheese and eggs (2.2%) accelerated.

Growth of prices of housing and energies slowed down.

Housing and energies descended from the position of item contributing the most to the year-on-year increase of consumer prices in Q2. Prices of housing and energies increased by 3.2% year-on-year, which is the least since Q2 2018. Slowdown was observed across the whole division of the consumer basket. Rate of growth of residential rents (3.7%) as well as imputed rent (2.6%) eased its pace. Slowdown of prices for electricity and heat, gas and other fuels (3.7%) was also an important factor. Prices of regular maintenance (3.3%) and other services associated with housing (4.3%) also grew slower than in the previous quarter.

Alcoholic beverages and tobacco also relatively strongly contributed to the growth of consumer prices.

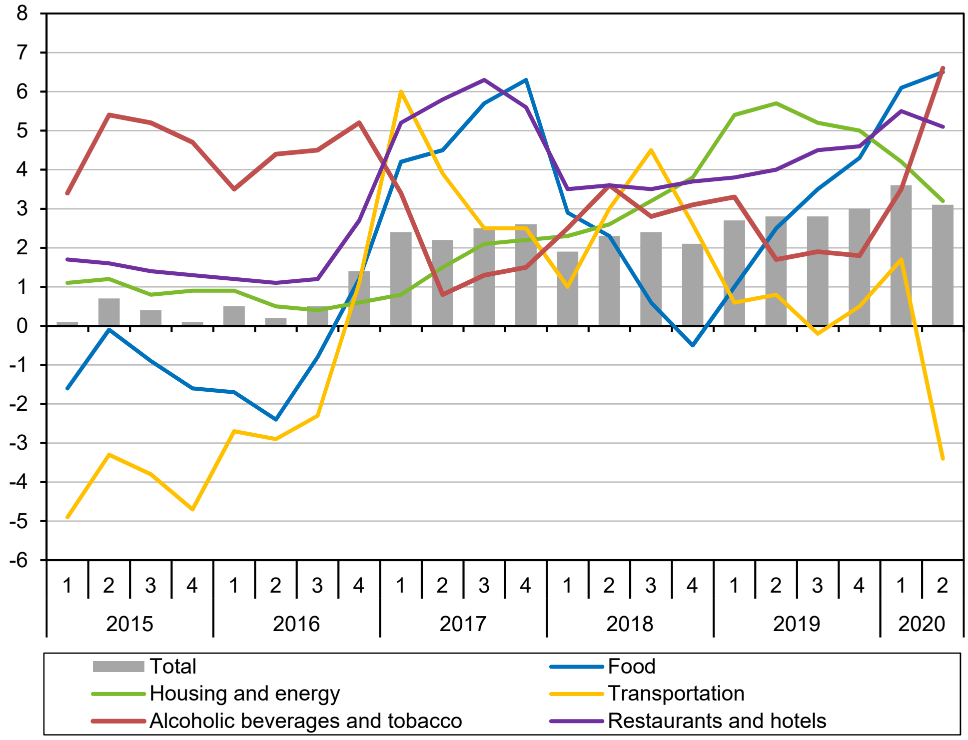
Prices of alcoholic beverages and tobacco also significantly influenced the development of consumer prices. They climbed up by 6.6% year-on-year in Q2. This division featured relatively strong growth already in Q1 (3.5%), for the reason of increase of the excise tax. It influences the alcoholic beverages as well as tobacco. While prices of alcohol went up immediately at the beginning of the year (4.5%), the development for tobacco was affected by pre-stocking with products with older tax stamps (2.6%). This effect however evaporated and sharp hike of tobacco prices occurred since May (7.5% for the whole Q2). Prices of alcoholic beverages also mildly accelerated (5.5%).

[32] Gauged by the GDP deflator.

Prices of transportation pushed the level down.

Among other divisions, which exerted significant influence on the growth of consumer prices, prices of food service and accommodation can be mentioned. They increased by 5.1% in Q2. Prices have reached relatively high year-on-year rate of growth here already since the end of year 2016 and further increase manifested since the beginning of this year. The prices of food service however grew faster (5.5%), pace of prices in accommodation notably slowed down in Q2 (2.5%). Recreation and culture also contributed to the growth of consumer prices (increase 2.0%). Mostly holidays with complex services stood behind it (5.1%), which raised prices markedly at the beginning of the year. Growth of prices of household equipment accelerated compared to Q1 (3.3%). Prices of transportation (–3.4%) had a marked counter inflationary effect. The reason was plunge of prices of passenger transport equipment operation by 11.1% (remainder of the March downturn of prices of oil to the historically low values). In contrast, the prices of purchase of motor vehicles, motorcycle and bicycles went up by 3.1%. Prices of transportation services rose by 2.0%.

Chart 9 Prices in the selected divisions of the consumer price index (year-on-year in %)



Source: CZSO

Mainly prices of transportation subdued the year-on-year growth of consumer prices in Q2.

Year-on-year growth of consumer prices in the EU[33] markedly slowed down in Q2 compared to Q1 and reached 0.6%. While the total addition to prices in the EU was 1.5% in Q1 and prices rose in all countries year-on-year, prices grew only in 13 states year-on-year in Q2. Slowdown of pace concerned all Union countries compared to Q1. Plunge of prices of transportation, in connection to the record slump of prices of oil stood behind it. Total prices of housing and energies decreased in Q2 as well. The prices grew the most in Poland (3.4%), the CR (3.3%) and Hungary (2.5%) in Q2. Consumer prices in Rumania (2.1%) and in Slovakia (2.0%) also featured notable increase. It represented a group of countries, who deviated from the rest of Europe with their price dynamics. They had common especially the high growth of prices of food and non-alcoholic beverages, but also alcoholic beverages and tobacco or housing and

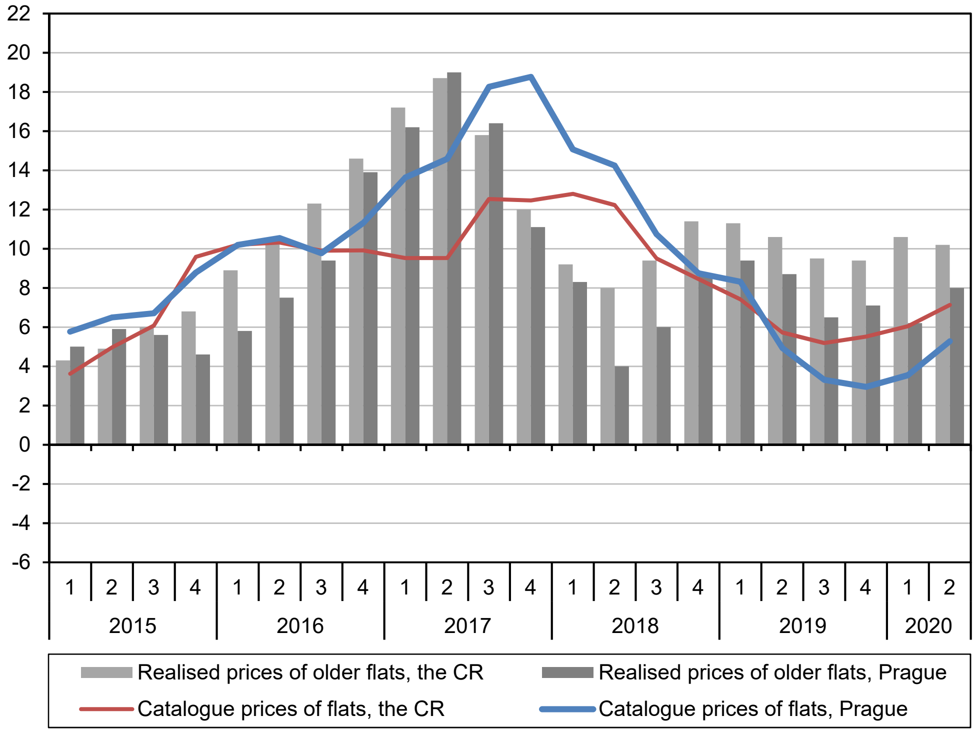
33 Based on the harmonised index of consumer prices. The index can differ from the published national results in both methodology and numbers.

energies. The largest year-on-year reduction of prices was recorded in Cyprus (–1.6%), in Estonia (–1.4%) and Slovenia and Greece (similarly –1.2%) in Q2.

Prices of flats grew by strong pace in Q2.

Economic crisis did not cause any turn in the development of supply prices of flats. Prices were raised by 1.6% in comparison to the preceding quarter. Year-on-year addition to supply prices of flats achieved 7.1% in Q2. Simultaneously, the very high year-on-year rate of growth for flats outside Prague was maintained (9.7%). Supply prices of flats in Prague increased by 5.3% year-on-year, which is the most since Q1 2019. Realised prices of older flats also kept relatively fast pace. They thus increased by 2.6% compared to Q1. Year-on-year addition was again more than one tenth in the whole CR (10.2%) and mainly the development outside of Prague stood behind it (10.8%). Realized prices of older flats in Prague increased by 8.0% year-on-year in Q2 and the growth rate slightly gained pace compared to the previous three quarters. The dynamics of realised prices of new flats in Prague gained new momentum. Following a small slowdown in Q2 2019, the year-on-year additions again oscillate around 10% this year. The increase reached 9.5% in Q2.

Chart 10 Prices of real estate (year-on-year change, in %)



Source: CZSO

Industrial producer prices fell in Q2, especially due to the plunge of prices of coke and refined oil products.

Industrial producer prices decreased by 0.6% in Q2. The price grew by 1.4% still in Q1. Turning point in the dynamics was observed already in March. The reason was especially the development for products and services of manufacturing. These recorded decrease by 2.3%, mainly because of coke and refined oil products[34]. Tied to the prices of oil, the prices of chemical substances and products were also falling (-14.6%). Basic metals and metal products (–1.3%) and wood, paper and printing (-2.1%) also pressed the prices down. In contrast, prices of food products, beverages and tobacco (3.0%) contributed to growth. Here however, the dynamics gradually lost pace during the quarter. Mainly the wage growth even pushed up the prices of furniture and other manufacturing products (4.8%, especially repairs, maintenance and

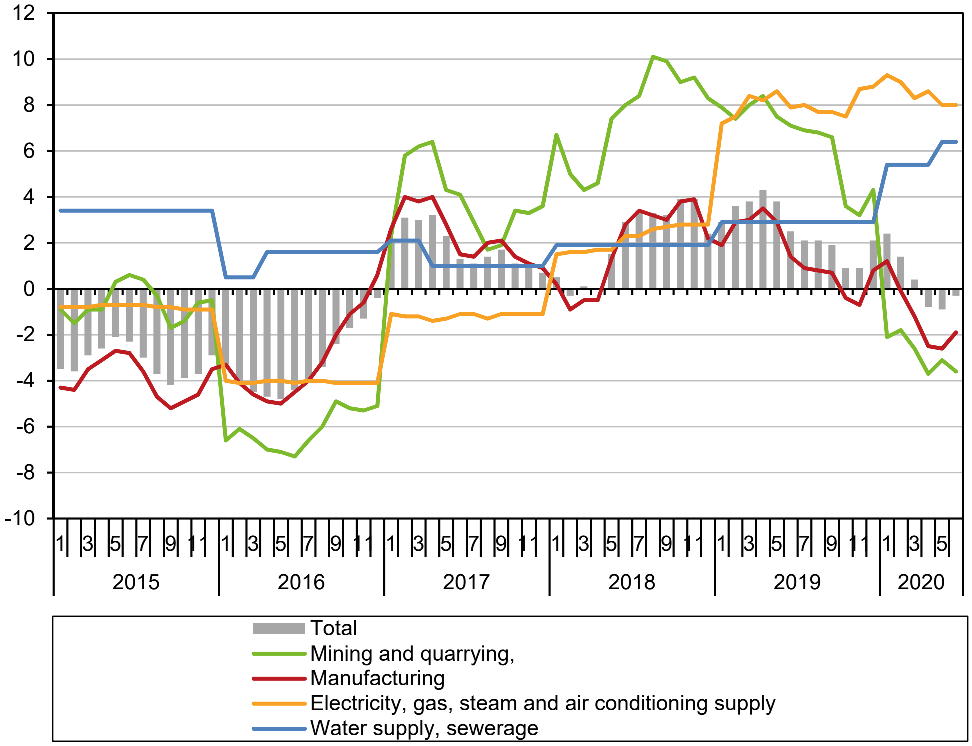
[34] Individual data.

installation of machinery and equipment). Prices of computers, electronic and optical equipment notably increased (3.7%). Transportation equipment also recorded a relatively strong addition (3.5%). Growth of prices of machinery and equipment (2.6%) and electrical equipment (1.7%) accelerated.

Plunge of prices in mining and quarrying continued.

Fall lasting from the beginning of year deepened in case of mining and quarrying (-3.5%). Prices of oil and natural gas plunged, and the decrease continued for black and brown coal and lignite. On the contrary, year-on-year growth of prices of electricity, gas, steam and air conditioning remains at high level (8.2%). Growth accelerated for water supply and wastewater management services (6.1%).

Chart 11 Prices of main groups of industrial producers (year-on-year change, in %, based on CPA classification)



Source: CZSO

Industrial producer prices were notably falling in the EU in Q2.

Industrial producer prices were falling in the EU in both Q1 and Q2. In Q2 nevertheless, the year-on-year decrease jumped to 4.1%. Strong slump of prices of oil, which was felt globally, was the reason similarly as in the CR. Notable fall of prices of mining and quarrying (–13.2%, mainly due to oil production) continued in the Union in Q2, but decrease of prices also deepened in manufacturing (–2.8%). Prices of electricity, gas, steam and air conditioning dropped by 9.1% year-on-year. Industrial producer prices increased only in Malta (1.4%), in Slovenia (0.3%) and in Slovakia (0.1%) year-on-year in Q2. The deepest fall was on the contrary in Lithuania (–9.6%), Spain (–7.7%) and Belgium (–7.5%).

Growth of prices of market services slackened in Q2.

Year-on-year growth of prices of market services slowed down to 2.1% in Q2. Slowdown of year-on-year dynamics was apparent across all branches. Storage and support service activities in transportation contributed the most to total growth of market services (year-on-year addition 5.0%). Further, it was services in the area of programming, consultancy and related activities (3.1%) and real estate services (2.9%, one of few branches, where the price growth slightly accelerated). Land and pipeline transport (1.4%), where mild growth is compensated by the large weight of the branch in the economy, also added to the total dynamics. Prices of insurance, reinsurance and pension funding rose by 3.1%. Services in the area of employment also increased their influence, strong year-on-year growth lasted (7.2%), even though slower compared to the previous quarter. Growth slowdown of prices of services can be linked for once to the milder growth of wages, which have great effect on the pricing, the downturn of demand is however also connected. It probably played a role in the substantial reduction of rate of growth of prices of advertising and market research (0.7%).

Prices of agricultural production decreased. Both prices of plant and animal production were falling.

Prices of agricultural output (including fish) fell by 3.2% year-on-year in Q2. Both prices of animal and plant production went down. Plan production featured moderation of decrease to –5.6%. Decrease continued for prices of cereals (–7.5%), mainly weight significant wheat (–7.3%). Prices of other cereals were however also falling (rye –11.4%, barley –8.4%). Reason can be seen mainly in the high comparative basis of the last year. Prices of industrial crop decreased by 2.6%, mostly under the influence of oil plants (-2.7%), where nevertheless the development of prices of oilseed rape seeds (growth by 5.7%) and poppy seeds (decrease by 34.2%) diverged. Prices of potatoes also dived (-19.3%), but due to the sharp increase in the past year (74.7% in Q2 2019) their prices remain at high level (30.4% above the average of year 2015). Prices of fruit also hiked up year-on-year (38.7%), especially apples (79.7%). Prices of animal production fell by 0.6%. The growth of prices of farm animals, especially pigs and piglets considerably moderated (11.2%). In case of other farm animals, the prices were falling (beef cattle -5.9%, poultry –1.5%). Price of milk were decreasing (–3.8%) and on the contrary prices of eggs went up (4.9%).

Koruna depreciation against both euro and dollar also pushed up the prices of both import and export.

Export prices went up by 2.6% year-on-year in Q2. Following two quarters of year-on-year decreases, the dynamics was again positive. It was a consequence mainly of sharp depreciation of the koruna exchange rate toward both euro and dollar. The influence of weakening played a key role, since after adjustment for exchange rate effects, the prices of export would fall year-on-year by 1.4%. Prices of food and live animals (year-on-year addition of 5.4%), beverages and tobacco (8.0%), semi-finished products[35] (1.6%), machinery and equipment (4.9%) and industrial consumption goods (5.7%) supported the growth of export prices in Q2. On the contrary, the year-on-year plunge of export prices of mineral fuels (–26.5%) notably deepened and prices of other materials[36] (–8.5%) was also falling. Decrease of price did not avoid also chemical substances and related products (–1.4%).

Import prices fell especially because of prices of oil.

Import prices fell by 0.5% year-on-year in Q2. Even here however strong koruna depreciation dampened the plunge of prices (after adjustment for exchange rate effects, the decrease was 4.4%). Mostly prices of mineral fuels (–40.1%), further chemical substances and related products (–2.1%) and other materials (–1.4%) were decreasing. Prices of beverages and tobacco imports were slightly cut (–0.8%). In contrast, significant increase occurred for prices of food and live animals (6.9%), machinery and equipment (4.9%) and industrial consumption goods (3.7%) in Q2. Large difference between the rates of growth of export and import prices also led to the increase of terms of trade to 103.1% in Q2. Terms of trade were positive for trade with mineral fuels (122.7%), beverages and tobacco (108.9%), industrial consumption goods (101.9%), semi-finished products (101.4%) and chemical substances and related products (100.7%). Trade with other materials (92.8%) and food and live animals (98.6%) reached negative terms of trade.

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[35] SITC 6 – manufactured goods classified chiefly by material

[36] SITC 2 – crude materials, inedible, except fuels.

6. Labour Market

Immediate impacts of the external shock on the labour market were considerably varied. They were reflected the most in fading of overall economic activity.

Even though the domestic labour market traditionally reacts to economic shocks with certain delay, the pandemic restrictions already managed to be markedly felt. More than two-month period of state of emergency struck into the whole first half of Q2 2020 and also in subsequent weeks the return to normal was taking place only very gradually. So far monitored impacts of this shock on the labour market were considerably varied (for example from the view of branch or position of persons in employment). Diverse intensity of impact also emphasised the testimonies of households (experiencing negative impacts in their employment as well as concerns regarding the growth of unemployment). The substantial downturn of economic activity expressed both by lower number of employed and also deeper reduction of hours worked were the most visible manifestations of the onset of economic recession in Q2. The on the contrary so far only mild growth of unemployment was connected to the stabilisation government programmes (Antivirus, care benefits) and with the fact, that part of persons, who lost work, evacuated the labour market (foreign workers, economically inactive). Worsened economic situation of businesses was evident by ceasing of growth of average wages in the majority of market branches and contrasted with the so far stabilised development in branches with the dominance of state.

Total number of employed shrank by significant 1.4% during Q2 following the stagnation at the beginning of the year.

While the total employment[37] stagnated in quarter-on-quarter expression in Q1 2020, similarly to the whole last year, it already dived by record 1.4% in Q2. In the preceding recession periods, the loss of employment positions was more gradual, simultaneously it however had longer term character[38]. The employment lowered by 1.9% year-on-year (the most after Q1 2010), it is however necessary to take into account, that the number of employed attained record level in the history of independent CR (5.44 mil.) last year. This decrease was caused nearly exclusively by employees, since the number of self-employed was falling slower (–1.5%)[39]. It can be perceived relatively favourably, because 60% of entrepreneurs (without employees) stated within the LFSS survey, that they experienced adverse impacts in their enterprise (financial difficulties, lower sales, volume of work or orders)[40]. Nearly three quarters of these affected at the same time considered the impacts likely temporary and possible to overcome (e.g. with the help of government programs).

Especially employees contributed to the year-on-year decrease of employment. Stronger reduction of places occurred in manufacturing and branches of services associated with tourism.

From the view of main branches, manufacturing where also due to "cooling" of agency employment 51 thousand of places decreased (3.5%), contributed to lower employment the most in the whole economy in Q2. Almost 43 thousand positions were cut in the services sector, it was however very unevenly distributed. Due to substantial impact of restrictions in the tourism area, the number of working in the grouping trade, transportation, accommodation, food service and restaurants reduced by 40 thousand, resp. 3.2%. Professional, scientific, technical and administrative activities (-4.4%) had the deepest relative reduction of places. It contrasted with the long term growth of employment in information and communication (+3.4%) and also in branches with the dominance of state (+1.6%), where it was the effect of recruiting in education, among other things also because of higher number of students in primary education.

Number of hours worked by employees returned to normal in June.

The effect of pandemic restrictions is plastically expressed by the decrease of number of hours worked in the economy. Based on the LFSS, it was 10% year-on-year in March, in

[37] Unless stated otherwise, data regarding employment are given in the national accounts' conception after adjustment for seasonal effects in this chapter.

[38] E.g. in years 2009 and 2010, the employment decrease lasted five quarters (it arrived at total –3.8%), in period 1997 to 1999 even ten quarters (–5.1%).

[39] Situation was however different in individual branches. 7% decrease manifested similarly in manufacturing, in grouping trade transportation, accommodation and restaurants. In contrast, the number of entrepreneurs expanded by one sixth in information and communication, it was also higher in construction (+1.5%).

[40] Small businesses were affected this way the most in accommodation, food service and restaurants (94% of entities in this branch), in education (95%), in cultural, amusement and recreational activities (74%) or in other services activities (86%), where is found for example hairdressing or repairs of products for personal use. Impact in the two most frequent branches among entrepreneurs was also significant – construction (56%) and trade (66%).

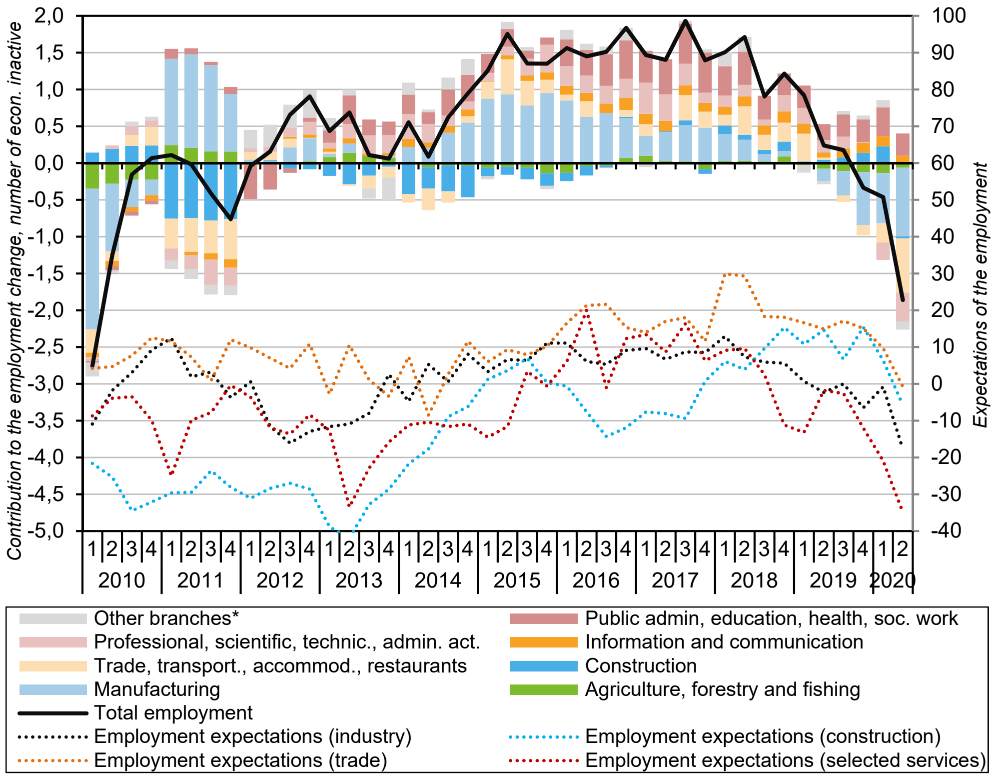
Expectations of employment development remained negative, especially in industry and majority of market services.

April it deepened to not yet seen 22% (31% for entrepreneurs). The descend decreased in May (to 8%) and July already signalled a return to paces from the turn of years 2019 and 2020 (–2%), which however was not completely valid for small businesses (–6%), where the effect of weakened demand was more evident. Expectations of businesses in the area of employment stayed in the majority of branches negative. It was valid for market services (except for trade), where the proportion of businesses anticipating growth of employment in the next three months was by 33 p. p. lower than the share of businesses planning to reduce employment levels in August 2020. This balance remained distinctly negative despite weakening pessimism also in industry (–12 p.p.). Businesses in trade (–5 p.p.) and mainly construction (+2 p.p.), where a large proportion of businesses did not anticipate changes in employment (87%) were in better situation. Still around 40% of construction firms considered the lack of workers as a barrier to growth even in the summer period.

Growth of the number of economically inactive drastically accelerated.

Changes on the labour market were reflected more than in the unemployment in enlarging the number of economically inactive H1. Even though the number of inactive was growing also for the most part of the last year, significant acceleration of the year-on-year pace occurred only this year. The increase was 59 thousand persons at the beginning of the year, already 86 thousand in Q2 (the most in the CR history). Mainly males aged 60 and more years (+25 thousand) and females aged up to 30 years (+33 thousand) contributed to the record growth. These groups typically more often utilise part time job contracts and temporary employment.

Chart 13 Total employment (year-on-year in %)**, contributions of main branches to year-on-year employment change** (in p.p.) **and expectations of employment development** (balance in p.p., right axis)



* Mining and energetics; Financial and insurance activities; Real estate activities; Arts, entertainment and recreation activities;
Note: Balance of expectations expresses the difference in p.p. between categories (growth vs. decrease of employment in the next three months). Data are seasonally adjusted and relate to the last month of the given quarter.
Source: CZSO (national accounts, business cycle surveys)

General unemployment rate increased only slightly; the rate grew faster for males.

General unemployment rate[41] went mildly up during Q2. It was 2.7%, while the difference between genders (0.3 p.p.) was one of the smallest in the monitored time series since year 1993. The unemployment of males rose by 0.8 p.p. since the beginning of this year, by 0.6 p.p. for females. It can seem surprising at first sight, since the recession hit more the branches of services with the predominance of employed women in its first phase. Onset of unemployment of females was softened by the option to draw care benefits[42] for the reason of closing schools and other facilities. Positive fact was that even long-term unemployed were still finding work. Their share on total unemployed neared 20% (the lowest level since half of 90s). However, the balance of expectations of growth of unemployment in the economy (in the upcoming twelve months) among households sharply hiked up and it got to the level last observed in year 2012[43] in Q2.

Expectations of households regarding the unemployment growth sharply hiked up.

Number of registered job vacancies only slightly fluctuated. Higher increase occurred in Prague and central Bohemia.

Number of job vacancies in the supply of labour offices did not feature any significant changes during H1. It equalled 334 thousand at the end of June and fell by 3.5% year-on-year (nevertheless by 15% for positions requiring higher than primary education). More than one third of positions was vacant for more than one year. Total supply of job vacancies decreased in manufacturing (in servicing machinery and equipment), in trade or administrative as well as support service activities. As a result of difficult mobility of foreign workers, the number of vacant jobs expanded in the primary sector. Growth of the total supply of job vacancies occurred in Prague (+15%) and central Bohemia (+12%), for the overwhelming part it consisted of low-qualification manual positions (for persons with primary education).

Total unemployment rate increased only slightly in majority of the EU states for H1. It grew faster for persons up to 25 years.

Mild reaction of the labour market to the economic shock can be observed in the majority of EU countries[44] for now. The unemployment rate[45] rose by 0.6 p.p. (without significant differences between males and females) during H1, it arrived at 7.1% in June. Only three states avoided decrease (Ireland, France, Italy), on the contrary Estonia, Latvia, Lithuania and Croatia registered growth within the rage of 2.5 to 3.5 p.p. Interestingly also, a lowest GDP decrease eventuated in the Baltic states compared to the EU members in Q2. Frequent employment in the affected branches as well as large share of more flexible job contracts led to higher increase of unemployment of young persons (aged up to 25 years) in the EU in H1 (+3.0 p. b. for females, +1.4 p.p. for males). It increased the most in Estonia (+14 p.p.) and Spain (+10 p.p.), where it reached maximum among the Union members (42%)[46]. Sweden, Luxembourg, Croatia and Portugal registered larger shift (by more than 7 p.p.). The shift was below 4 p.p. in the CR, unemployment still ranked among one of the lowest even in this age group in the whole EU (CR 8.6%, Germany 5.7%, EU 16.9%).

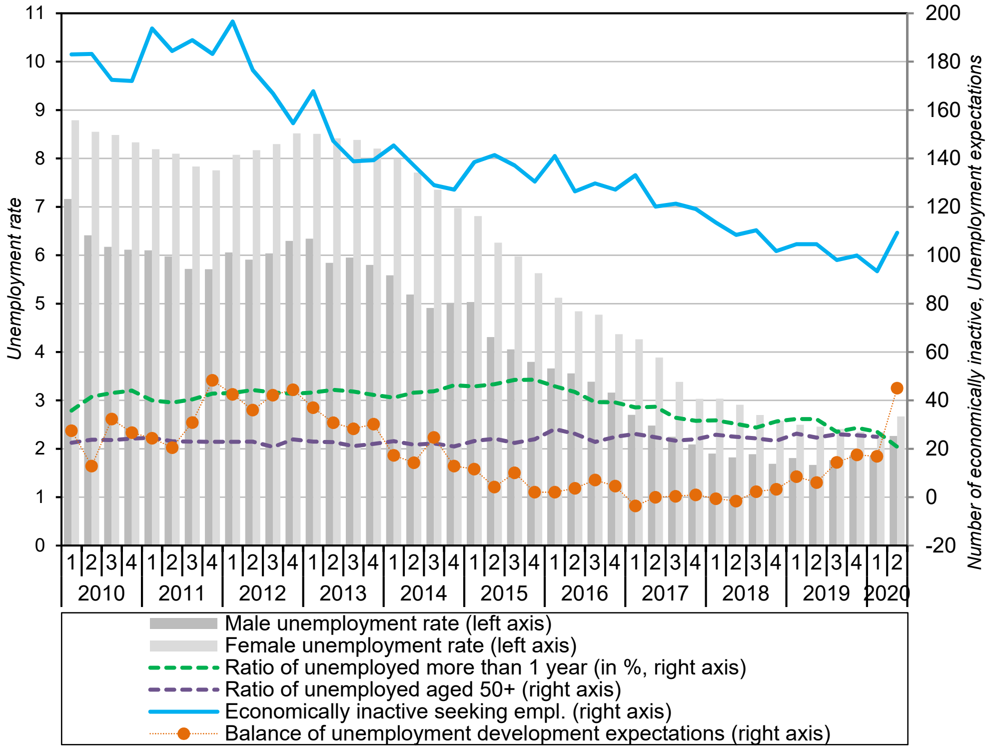
So called hidden unemployment increased significantly in the EU already during Q1.

Differences between the EU states in the existing impacts of the shock on the labour market were influenced by the speed as well as intensity of adopted counter pandemic measures, branch structure of the economy as well as extent of government stabilisation measures aimed at both employers and small-scale entrepreneurs. Data for Q1 already suggest, that the transfer of employed among economically inactive was the most significant flow on the Union labour market[47]. Part of these inactive can be at the same time regarded as hidden

[41] For persons aged 15–64, value after seasonal adjustment. All given unemployment data are sourced from the data of Labour Force Sample Survey.
[42] Total drawing of care benefits was 9.1 CZK bn from March till July of this year, it was only 0.6 bn in the same period of the last year.
[43] According to data from business cycle surveys, e.g. persons with higher level of education, persons aged 50 to 64 or persons working in groups based on the classification ISCO 1-5 (managers, specialists, technical and specialised workers, workers in services and trade) recorded higher than average balance (+47 p.p.) in August 2020. Higher expectation of unemployment does not necessarily mean expectation of worsened financial situation of the given person or household.
[44] It was also valid for example about Japan. On the contrary, the labour market reacted very fiercely in the USA. While unemployment reached here 4.4% in March, it accelerated to 14.7% in April. Only small correction occurred in the subsequent months, but the June value still exceeded 11% and it was by more than 1 p.p. above the level from the recession peak from years 2009 to 2010.
[45] Relates to persons aged 15–74, all data regarding unemployment describe reality after seasonal adjustment.
[46] It reaches high level also in Greece in the long term, for which the most current this year´s figure relates to May (37.5%).
[47] According to the LFSS, it concerned 3.9 mil of citizens (aged 15 to 74 years), which were employed in Q4 2019 and were counted among inactive in the following quarter. The flows between inactivity and unemployment were in the same period nearly equal (3.2, resp. 3.3 mil.). Relations between employment and unemployment appeared still mildly in favour of employed at the beginning of the year (+0.4 mil.), however

unemployed[48]. Their ratio to the total number of economically active increased from 6.8% to 7.4% compared to Q4 2019 and attained high values even compared to "classical" unemployment in some states (Italy, 14.7%, Finland 10.6%), however very low 0.9% in the CR.

Chart 14 General unemployment rate (in %), **ratio of long-term unemployed and persons aged 50 and more among unemployed** (in %), **economically inactive willing to work** (in thousand)* **and unemployment expectations of households** (in %)**



Note.: Figures regarding the unemployment rate are seasonally adjusted, other data are not.
*Persons not in employment, not seeking work, but expressing the willingness to work.
**Seasonally adjusted balance of expectations of unemployment in the next 12 months (difference between percentage frequency of answers of households "growth" and "decrease" expressed in percentage points. Data relate to the last month of the given quarter.
Source: CZSO (LFSS, business cycle surveys)

Size of average wages dropped by 3.1% quarter-on-quarter and partially reflected the deeper slump of the number of hours worked.

Restriction of operations as well as temporary closing of some businesses especially in the area of market services or manufacturing (as a consequence of both quarantine measures and longer-term decrease of demand) must have manifested also in the wage area. The size of average wages (after seasonal adjustment) dropped to record 3.1% in comparison to the preceding quarter in Q2 (it still grew by 1.1% in Q1). In the year-on-year comparison the wage growth nearly halted (+0.5%), lower dynamics was comparable in the 20year time series only during year 2013, when however, the rates of growth were artificially oscillated[49]. Weaker wage growth rates partially mirrored the steeper fall of average hours worked[50].

In the year-on-year expression, mild growth of wages persisted. Factors preventing fast

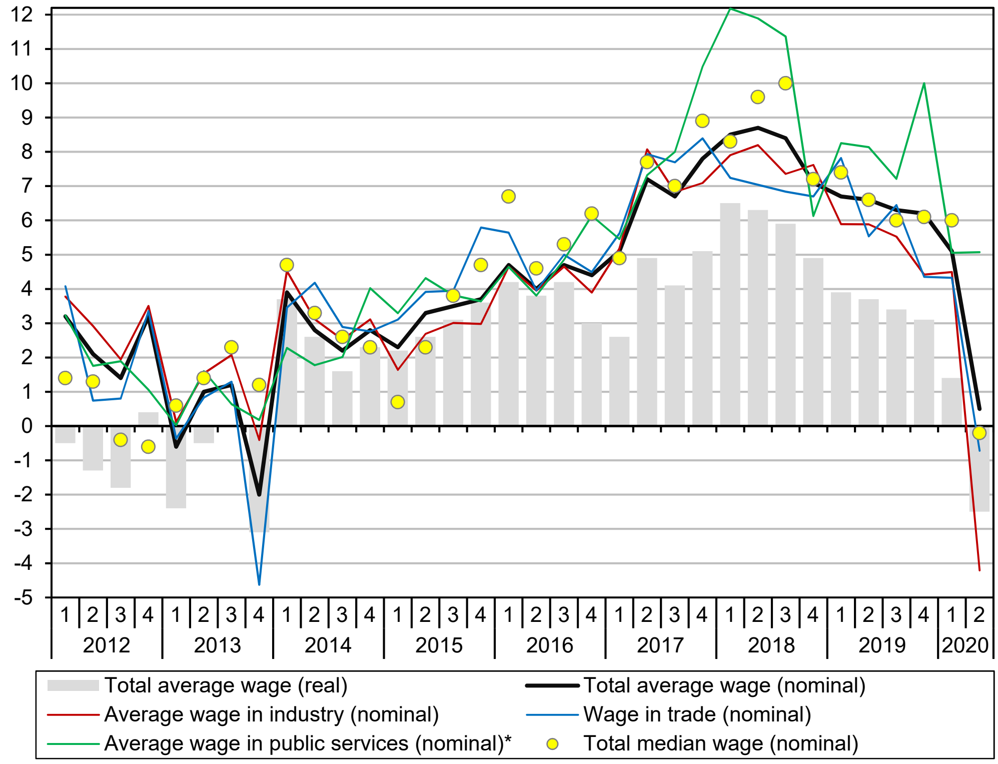
The administrative influences (raising of the minimal wage and bands of guaranteed wages) as well as the tense condition of the labour market at the beginning of the year (characterised among other things by the lack of labour force), which partially prevailed in

as the first estimations from the national accounts clearly indicated, a sharp decrease of the number of employed (year-on-year as well as quarter-on-quarter by nearly 3%) occurred in the EU in Q2.
[48] It concerns persons ready to enter employment, who however do not actively seek job, further persons who seek employment, but are not able to join it within 14 days (because of this they do not fulfil condition of being ranked among unemployed) and finally also so called underemployed i.e. those who do have a job, however work involuntarily part time (e.g. for the reason of lack of work at their employer).
[49] It was a consequence of transfer of payment of non-mandatory wage components of part of high-income workers for the purpose of tax optimization.
[50] State partially contributed to businesses afflicted by the impacts of the coronavirus crisis after fulfilment of certain conditions (e.g. preserving job positions) on employee wages (programme Antivirus). Persons were drawing these wage compensations due to work barriers caused by the pandemics. On the contrary persons who did not work for the reason of drawing of care benefits or ordered quarantine received transfers from state, which are methodically not part of wages (their drawing thus worked against the growth of the average wages).

downturn of the wage dynamics still worked.

some branches also in the summer period, prevented deeper reduction of the size of earnings. Rigidity of wages (existence of longer-term internal contracts of enterprises regarding the growth of wages or the tariff system in the public sphere) also played a role. It cannot be excluded, that the worsened economic situation of businesses could have been reflected also in the reduction in the area of non-wage employee compensations this year.

Chart 15 Average nominal and real wage and wage median (year-on-year, in %)



* Includes branches: Public administration, defence, social security; Education Human health and social work activities; Arts, entertainment and recreation activities.
Source: CZSO

Wage development at the level of branches was very varied in Q2.

Markedly uneven primary impact of counter pandemic measures as well as different flexibility of various segments of the labour market (e.g. tie of the volume of earnings to the number of hours worked) were reflected in the very differentiated development of wages at the level of individual branches in Q2 2020. It is not surprising, that the average wages fell the most in the strongly hit branch accommodation, food service and restaurants (–11.8%) year-on-year. This development was in addition amplified by even deeper reduction of the registered number of employees, volume of paid out wages thus dropped by one quarter here. The average wage went down by 6% in the real estate activities. Higher wage basis of the last year and also the swift growth of employment this year (still it presented the smallest branch of the services section – given the number of employees) both had an effect. Transporting and storage also belonged to the strongly affected branches, where the decrease of wages (–1.7%) was overshadowed by deeper reduction of employee positions (–4.2%). Already last year signalled a light decrease (mainly of employment) in this branch, specifically in connection to weakened performance of industry as well as associated demand in the freight transportation. The decrease of wages as well as employment was compared to the before mentioned branch approximately only one half in trade. The situation here was likely very different, depending on the size of the business. Adverse development was notable in the branch other services activities (including for example hairdressing), total volume of paid out wages shrank by more than 8%. It was also lower especially due to the reduction of the

Restrictive measures impacted the most accommodation, food service and restaurants, where the volume of paid out wages dropped by one quarter.

number of workers by 6.5% in cultural, amusement and recreation activities[51]. Administrative and support service activities, which are in the conception of enterprise statistics formed mainly by the agency workers, is also necessary to include among more hit branches. Dismissals of low qualified workers[52] led here next to the increase of the minimal wage to the growth of the average wage (+4.2%). This development was closely tied to the situation in manufacturing. Several weeks interruption of production mainly in the companies of motor vehicle industry resulted in the considerable year-on-year decline of hours worked by employees (–13.6%) in Q2. Volume of paid out wages slumped by one tenth, which was equally caused by the loss of job positions and lower average wage.

Energetics, information and communication and public services maintained brisk growth of the average wages.

Construction was not at first affected by the onset of recession, both employment and average earnings stagnated here in Q2. Energetics, where as in the only main branch the year-on-year growth of wages did not slacken compared to the pace from the same period of the last year (+5.3%) also prospered. The size of average gross monthly wage approached the boundary of 50 CZK thousand here, it featured the largest increase among all branches (by 2 471 CZK). Employees of information and communication were also by 3.5% better off, their earnings were already 3.5 times higher compared to workers in branch accommodation, food service activities and restaurants. The wage growth ceased in financial and insurance activities this year (–0.6%). The impact of high last year basis, when the pace of average wages exceeded 8% was also evident next to the decrease of the profitability of the financial sector. The wage growth slightly overstepped 5% in the services with the dominance of the public sector and the achieved wages level surpassed the level of the whole economy (34 271 CZK) by one tenth in Q2. Pace of wages was also influenced by the extraordinary increase of compensations for overtime work in some very busy fields (health care).

Total wage differentiation considerably widened in Q2.

Above mentioned development led to the widening of scissors of wage differentiation. While the lowest wage decile fell by 1.7% year-on-year in Q2, value of the highest decile increased by 2.2%. The wage median recorded the first decrease since the end of year 2012 (–0.2%). It was falling faster for males (–1.0%), still the achieved median earnings of males exceeded those of females by 16% (resp. near 5 thousand crowns).

Real wage decreased after more than six years.

Weaker dynamics of nominal wages during the first half of year 2020 contrasted with the swift growth rate of growth of consumer prices not losing strength. Average wage dropped by 2.5% in real terms in Q2. More than six years prevailing growth of the purchasing power of employee earnings was thus interrupted.

[51] The average wage was falling slower here in Q2 (by 1.3%). It was also connected to the fact, that approximately half of employees belongs to the so-called wage sphere in this branch and their compensations are then tied to the public budgets.
[52] Number of employees fell by 12% here year-on-year in H1 2020, similarly to the crisis year 2009.

7. Monetary Conditions

Key monetary policy-relevant interest rates were again decreased in Q2.

Set up of key monetary policy-relevant rates considerably changed together with the development of the economic situation during H1. Given the strengthening inflationary pressures, the repo rate was increased from 2% to 2.25%[53] at the beginning of the year. This level however held only shortly. The rate was reduced to 1% in March and further down to 0.25 % in May, the lowest value since November 2017. The discount rate was technically zero (0.05%) at the end of June and the Lombard rate attained 1%. Koruna foreign exchange against both euro and dollar stayed at higher level during the whole April and large part of May following marked March depreciation. Koruna foreign exchange per euro remained above 27 CZK/EUR for the major part of this period. The foreign exchange again gradually appreciated to 26.65 CZK from 20th May till 2nd June. Subsequently it remained near this level until the end of month. Development in case of dollar was very similar. The koruna foreign exchange often moved above 25 CZK/USD during April and May. Koruna again strengthen up to 23.47 CZK/USD in the period from 20th May to 5th June and it was mildly depreciating in the direction of 24 CZK per dollar until the end of June. Notable deprecation of koruna towards other currencies meant strengthening of the inflationary pressures from abroad.

Koruna foreign exchange per both euro and dollar again appreciated after the March weakening.

Interbank interest rates and also the yields of government bonds sharply dropped.

Changes of the monetary policy-relevant rates led to fast decrease of the interbank interest rates. The three-month PRIBOR thus attained 2% towards the end of March and it was 0.34% at the end of June. Interest rates on government bonds were also falling, specifically for all types of maturities. The average interest thus decreased from 1.27% to 0.08% for bonds with maturity up to 2 years, it was from 1.23% to 0.52% for maturity up to 5 years and the rate moved from 1.28% to 0.86% in case of bonds with long term maturity from the end of March till the end of June. Rates on the government bonds issued by the area followed similar pattern of development. Both short term and medium-term maturities had negative interest rate towards the end of June (–0.36% for short term, –0.04% for medium term). The average interest on long term bonds was 0.35% in the euro area towards the end of June.

Interest rates on the client accounts also reacted to the new conditions. Decrease of interests on deposits with agreed maturity was also connected to the transfer of financial funds to the non-term deposits.

Interest rates on some types of deposits also very fast reacted to the new situation. The average interest rate on the current accounts of households was 0.03% at the end of this year's June (it lowered by 0.01 p.p. compared to March). Interests on the current accounts of households stays at the nearly zero level already more than four years and did not react in any way to the previous increase of the monetary policy-relevant rates. Interests on deposits with agreed maturity sharply slumped. Total average fell since the end of March (1.43%) to 0.6%. The decrease affected all types of maturity, the most however maturity up to and including 1 year (decrease between March and June from 1.38% to 0.37%) and above 1 year till 2 years (from 2.07% to 1.53%). Rates on the current accounts dropped also to the non-financial businesses (from 0.16% to 0.04%). Slump of interest rates on deposits with agreed maturity for non-financial businesses was even stronger than for households (from 1.36% in March to 0.16% in June). It thus was not surprising, that the total volume of deposits with agreed maturity was by 1.3% lower year-on-year at the end of June, while non-term deposits strengthened by 13.3% (the most since September 2017).

Consumption possibilities were limited in Q2, which was also evident on the development of the volume of provided consumer credit.

The access of households to the credit financing was also made cheaper in Q2. The average interest rate of consumer credit decreased by 0.26 p.p. to 7.89% between March and June and it moved below the 8% boundary for the first time. The average interest on mortgages also decreased (–0.13 p.p. to 2.42% at the end of June). The

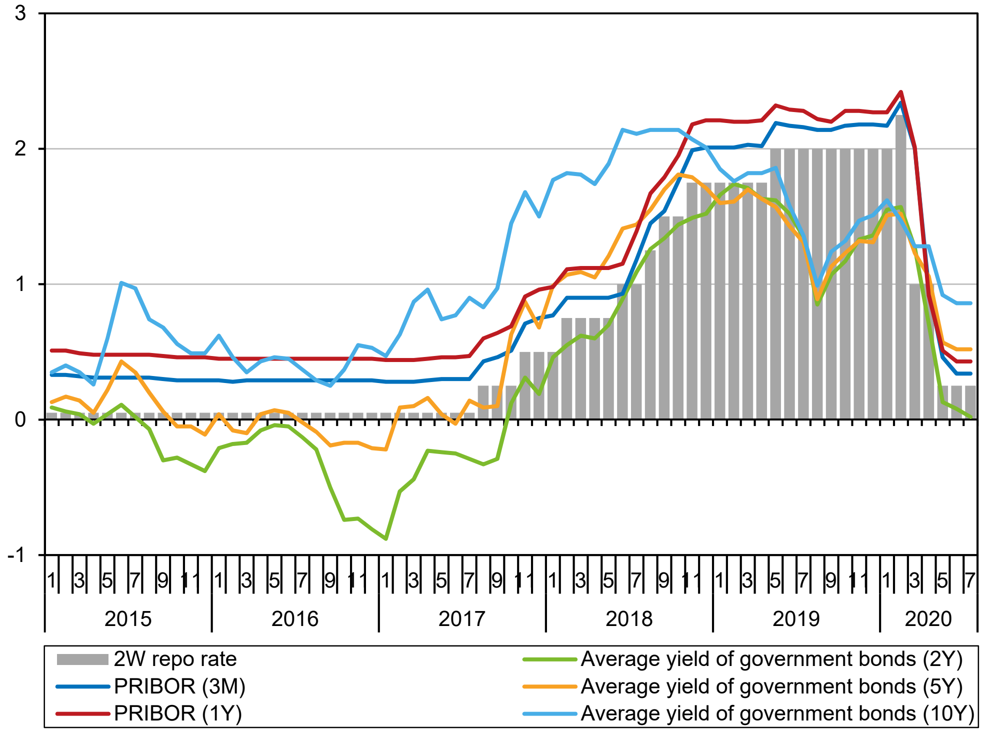
[53] Unless stated otherwise, the source of data in the chapter is the Czech National Bank database ARAD. Values of foreign exchange rates are also sourced from the CNB.

reduction was the most significant for fixation of the rate up to 1 year, but the cut occurred also in case of fixation above 1 year till 5 years and above 5 years till 10 years. Only interests on mortgages with fixation above 10 years went up in Q2. Ongoing restrictions had impact on marked slowdown of the year-on-year rate of growth of the volume of consumer credit in Q2. While in the previous half year the rate was 9%, at the end of June, the volume of provided credit was by 6.3% higher year-on-year. Regarding mortgages, the decrease did not manifest. Volume of provided mortgages rose by 7.9% year-on-year, the pace thus slightly accelerated.

Access to credit made cheaper for non-financial businesses. Uncertain environment however also led to moderation of the credit dynamics.

Interest rates of credit for non-financial businesses were cut across the board since March till June. The most for credit above 30 CZK mil (–1.03 p.p. to 2.07%). Credits with the volume between 7.5 to 30 mil recorded a decrease of average rate by 0.89 p.p. to 2.54%. The interest was decreasing the least for credit up to 7.5 CZK mil (–0.67 p.p. to 3.78%). Year-on-year growth of the total volume of credit and receivables of non-financial businesses slowed down in Q2. In comparison to the end of June 2019, the volume of koruna credit and receivables went down by 2.8%. Volume of credit in foreign currency on the contrary increased year-on-year by 21.7%. Growth of the volume of provided credit slowed down in manufacturing (3.5%), construction (4.8%) and in wholesale and retail, repairs and maintenance of motor vehicles (1.2%). The volume of credit to real estate activities grew on the contrary very fast (12.3%; very substantial addition 10.3% was recorded already in Q1). Part of the addition in manufacturing or financial and insurance activities is however also connected to the March depreciation of koruna, which was reflected in the recalculated value of credit in foreign currency. The volume of credit in accommodation, food service and restaurants also reached high year-on-year addition (10.2%) in March, and the year-on-year increase reached 12.5% at the end of June. The volume of credit for public administration, education, health and social work grew notably during Q2 (value was by 16.9% higher year-on-year at the end of June). Volume of credit was lower year-on-year for information and communication (–6.9%), financial and insurance activities (–2.0%) and a series of cuts continued also for mining and quarrying (–0.9%) at the end of June.

Chart 15 Market interest rates (in %)



Source: CNB

8. State Budget

State budget slumped to the deepest deficit in the contemporary history in Q2.

State budget (SR)[54] ended in considerable deficit of 195.2 CZK bn for H1 2020. Compared to the so far record half yearly value from year 2010, which already for the most part reflected the impacts of the deep economic recession, this year´s deficit was more than twice and a half higher. Even though the SB budget struggled with deficits in all months of this year up to now, the May deficit (64 bn) contributed the most to the half yearly result. Impacts of intensive counter pandemic measures were already considerably felt during Q2, both on the revenue and outlay side of the budget. It inevitably brought the need for fundamental revision of the originally approved yearly budget deficit[55].

Downturn of economic activity together with measures to strengthen the liquidity of firms led to 12.6% decrease of state-wide tax collection.

Total revenues of the SB fell by 5.9% year-on-year in H1, resp. by 44 CZK bn. Within H1, it presented the first decrease since year 2017, which was however influenced by the slump of the European subsidies, which occurred at the onset of new programme period at that time. The tax revenues of the SB itself lastly fell year-on-year in H1 2012. Depth of the downturn of economic activity also proves the decrease of state-wide tax collection (at the level of all public budgets) in the first this year's half, which was 12.6%, resp. 65 CZK bn (without insurance on social security). While the collection fell „only“ by 10.2% in H1 2009. This year's collection however included the significant effect of measures on the strengthening of liquidity of firms affected by the slump of sales[56]. Decrease of the total revenues of the SB was dampened by the growing inflow of funds from the EU budget.

Marked deprivation of collection of direct taxes affected negatively the most the total tax collection.

Collection of the corporate tax, which was by one quarter lower year-on-year (it still registered weak growth by 1.6% in Q1), contributed the most to the decrease of half yearly tax SB revenues. Above mentioned tax measures played a major role. Collection of income taxes of natural persons slumped by 18.5% in H1. Its size was affected by the paid out compensation bonuses (especially self-employed – in the size of 21 CZK bn), lengthened deadline of filing the tax returns by tax payers, growth of number of persons drawing care benefits as well as decrease of volume of paid out wages in the economy due to the reduction of employment together with lowering of the growth pace of the average wage.

Lower VAT collection reflected the deeper March and April decrease of retail sales. Decrease of collection nearly halted in June.

From the weight dominant tax – VAT – flew into the SB by 6.1% (resp. by 8.2 CZK bn) less year-on-year in H1. This decrease reflected especially the downturn of retail sales in March and April, since the collection of taxes grew during the first two months of the year. The June VAT collection itself did not significantly lag behind the last year´s level anymore (–1.6%). Half yearly collection was also adversely affected by the deferral of part of payments (in the amount of 5.8 CZK bn), lowering of tax tariff for some items[57] also had an effect. Higher expenditures of the government sector had the opposite influence.

Lower transport performance manifested in 10% decline of collection of tax on mineral oils. Limitations of relations with non-residents also affected the weaker collection of

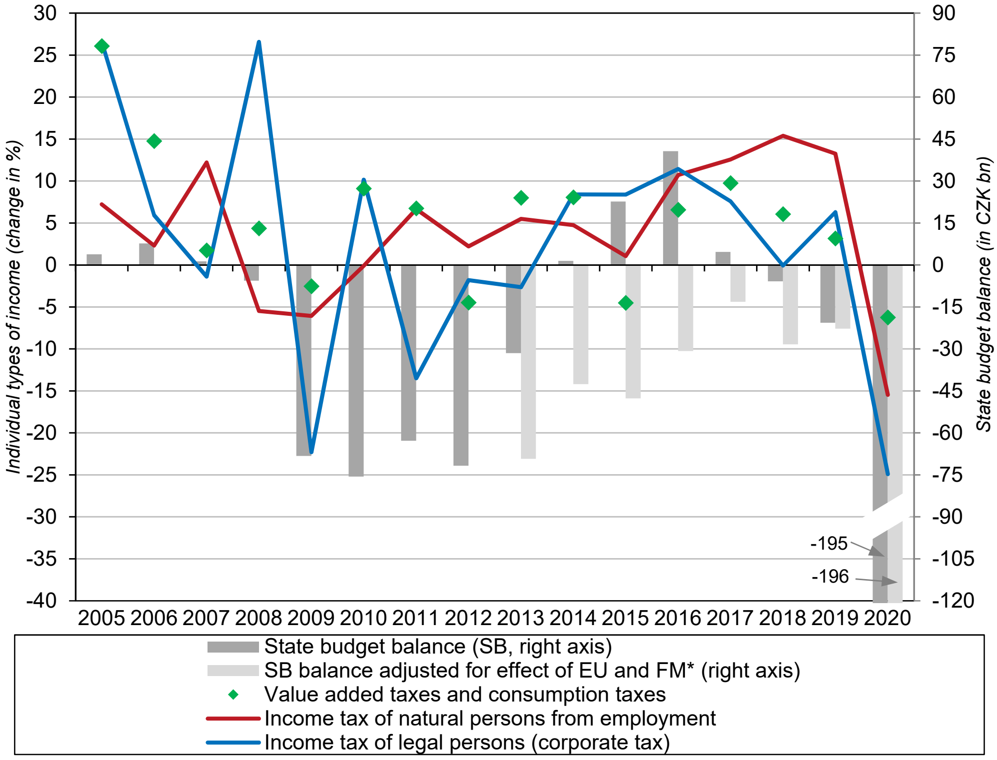
Total collection of the SB from consumer taxes weakened to 6.5% year-on-year in H1 (resp. nearly 5 CZK bn). Especially the fallout of collection of tax on mineral oils (by 10%) due to the considerable reduction of transport performance (including transit transport) had an effect. More detailed data of the CZSO regarding the consumption of oil products suggest, that the largest downturn occurred during April[58]. The counter pandemic measures also afflicted the weaker collection of other consumer taxes, for example for beer (by 8%), where

[54] Unless stated otherwise, all data related to the state budget stem from the data of the Ministry of Finance regarding the cash fulfilment.
[55] This deficit in the amount of 40 CZK bn stemmed from Act on the state budget of the CR (approved on 4th December 2019). Acts expecting deepening of the deficit to 200, resp. 300 bn were approved in the course of March and April 2020, deficit 500 bn was approved at the beginning of July.
[56] It was mainly the remission of the June advance payment for both the income tax of natural persons (NP) and legal persons (LP), possibility to lodge the tax returns of NP and LP for year 2019 and its payment only on 18th August, paid out compensations bonuses (especially self-employed) and also longer term for part of VAT payments. According to the MF estimation, the above-mentioned amendments led to decrease of the state-wide tax collection by 53 CZK bn in H1.
[57] It concerned mainly the regular public transport, heat, air conditioning and also food services.
[58] In April, the consumption of diesel decreased by one fifth year-on-year, for petrol even by one third. The May decrease moderated to 9%, resp. 19%, for kerosene however the unprecedented fall further deepened (from 73% to 89%). Even though the consumption of all main oil products grew for the first two months of year 2020 (e.g. diesel +1.8%, petrol +0.4%).

tax on beer or tobacco products.

higher consumption of bottled beer was not adequate to offset lower slump of draught beer or tobacco products, where the collection despite increased tax tariff fell 3% (among other things due to temporary slump of across the border purchases from Germany and Austria). Collection of tax on alcohol, where the effect of tariff growth was hampered by lower consumption, also did not fulfil the budget anticipations, also as a consequence of the dramatic slump of the arrival tourism in the whole Q2.

Chart 16 State wide collection of selected tax incomes (year-on-year in %) **and state budget balance** (in CZK bn, right axis) **in accumulation for H1**



*Balance adjusted for resources on programmes from the EU budget (incl. financial mechanisms), which were pre-financed from the SB and are subsequently reimbursed from the EU and FM budgets. Data available since year 2013.
Source: MF CR

Rate of growth of total SB outlays accelerated. It was driven by higher current outlays as well as investment.

Total SB outlays increased by 17.0% year-on-year in H1, resp. by 130 CZK bn (by +13.0% for Q1). Even though the double-digit growth was recorded also during years 2018 and 2019, this year´s half yearly pace belongs to the highest in the history of independent CR[59]. The achieved rate of growth was more than quadruple compared to the originally approved budget (from the end of year 2019). Mainly current outlays contributed to the growth (+15.5%, +112 bn), more than one third of their addition was attributed to direct SB outlays connected to counter pandemic measures[60]. It was evident the most in the acceleration of non-investment transfers to business entities (+83%, from more than one half driven by the compensation of part of wages to employees within the Antivirus programme), non-investment purchases and associated outlays (+27%, nearly exclusively due to the purchases of protective aids and materials) or current transfers to state funded organizations (+23%, in two thirds due to the partial debt relief to hospitals and strengthening of transfers in the area of cultural activities).

More than one third of current outlays growth was linked to the counter pandemic measures,…

… higher drawing of social benefits, especially non pension

Measures stimulating incomes, resp. household consumption (social benefits, wages in the public sector) remained the dominant source of SB current outlays growth. Current transfers

[59] Within the first half year, the total budget outlays grew the most in the period after year 2000 in year 2008 (by 12.5% year-on-year), when they were however accompanied by high inflation (year-on-year growth of consumer prices was 6.3% for the whole year 2008).
[60] For H1 2020 it was especially programme Antivirus (13.6 CZK bn), care benefits for employees and self-employed (7.9 bn), purchase of protective aids and other outlays in connection to covid-19 (9.6 bn), debt relief for selected hospitals (6.6 bn) and increase of the state payment per insured person (3.0 bn).

however also contributed similarly.

to regional budgets strengthened by one seventh year-on-year (mainly due to increase of wage resources to employees of primary as well as secondary schools and also in the area of social care). Wage outlays in the central government institutions featured more modest growth (+4.1%, four year minimum). Even though the year-on-year rate of growth of outlays on social benefits increased by 13.3% and strengthened by more than one half compared to the last year, proportion of benefits on all SB outlays decreased already third year in a row (to record 37.9%). For the first time after year 2014, the growth of social transfers was driven primarily by non-pension benefits, which expanded by one third year-on-year (to 86 CZK bn). Paid out benefits of sickness insurance accelerated (+10.2 bn)[61], which was the result from two thirds of the payment of care benefits provided for the reason of closing schools and other institutions. The increase of total morbidity however also had an effect (particularly due to the cancelled grace period), drawing of parental benefits was also slightly higher. State social care expenditures strengthened by one third (+6.6 bn), nearly exclusively due to the effect of legal increase of the parental allowance. Long term growing care allowance also accelerated (by one fifth, resp. 2.9 bn). The state expended more on the unemployment benefits for second year in a row. Even though the levels of registered job applicants have not expanded so far[62], the volume of paid out benefits increased by 0.9 bn, resp. by one fifth compared to last year´s H1 (the most after year 2009)[63]. On the other hand, the total financial situation of households has not markedly worsened so far also thanks to the extraordinary public transfers. It is also proved by the six years lasting year-on-year decrease of the volume of paid out benefits of material deprivation assistance (by 61% in total, by 2% this year)[64] or decrease of paid out child allowances.

Swift growth of outlays on wages in both education and social care continued.

Total financial situation of households has not markedly worsened also thanks to the extraordinary public transfers so far.

Revenues of the pension insurance fell for the first time after year 2013. Pension account deficit reached six year maximum.

Year-on-year growth of expenditures on pension attained 8.0% in H1 and only slightly lagged behind the last year´s pace (8.8%), which however was the highest after year 2009. Given the stagnation of the total number of persons receiving pensions (including old age pensioners) the effect of legislative amendments became fully evident[65]. Revenues of the pension insurance went down (by 1.1%) for the first time after year 2013. It was the consequence of worsened situation on the labour market (lowering of employment as well as number of hours worked, slowdown of growth of average wages), but also the budget measures aimed at the support of small businesses[66]. Pension account balance[67] thus returned to deficit after two surplus years. It amounted to 12 CZK bn in Q1, which presented the worst result in the last six years.

Investment growth from the SB further accelerated, mainly thanks to higher outlays on transport infrastructure.

With the approaching end of the current programme period of the EU, the drawing of European funds gradually accelerates in the CR. Total capital outlays of the SB were 64.5 CZK bn in H1 and increased by two fifths, resp. 18.7 CZK bn in H1. Mostly investment from national resources (+13.7 bn) shared in this growth, which was associated with higher outlays on transport infrastructure. Still the funds on common programmes of the CR and EU (35.5 bn) formed predominant part in the total volume of investment. Proportion of investment on all SB outlays was expanding third year in a row and reached 7.2%, which was the most in the last five years. Net position of the CR towards the EU budget was +50.1 CZK bn in H1 and doubled

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[61] It had adverse effect on the considerable year-on-year deepening of the sickness insurance deficit (from –1.5 CZK bn to –13.0 CZK bn). It was even larger than for pension insurance for H1 2020.
[62] The ratio of unemployed applicants (on population in the productive age) was 3.7% at the end of June and it rose by 1.1 p.p. year-on-year. Number of applicants entitled to unemployment benefits expanded from 68 to 93 thousand, their proportion on all unemployed remained the same for the last two years (35%).
[63] It was the effect of development mainly in May and June 2020, when the volume of unemployment benefits enlarged by 47%, resp. 71% year-on-year.
[64] The development in Q1 2020 stood behind the favourable result (–11%), the volume of claimed benefits already increased year-on-year in Q2 (+7%).
[65] Basic pension assessment increased by 220 CZK (3 490 CZK), percentage assessment increased by 5.2% and an additional amount of 151 CZK. Based on the CSSA data, the average monthly old age pension (alone) was 14 427 CZK in Q2, by 1 019 more year-on-year.
[66] It was related to the cancellation of minimal advance deposit for self-employed on social security insurance with the estimated budget impact in the amount of 4.8 CZK bn (based on the MF).
[67] It is expressed as the difference between revenues and expenditures on pensions from the SB. Expenditures on administration of the pension insurance system are not included in the expenditures (they arrived at 6.3 CZK bn based on the MF data in 2019).

Positive balance of the CR towards the EU budget doubled year-on-year.

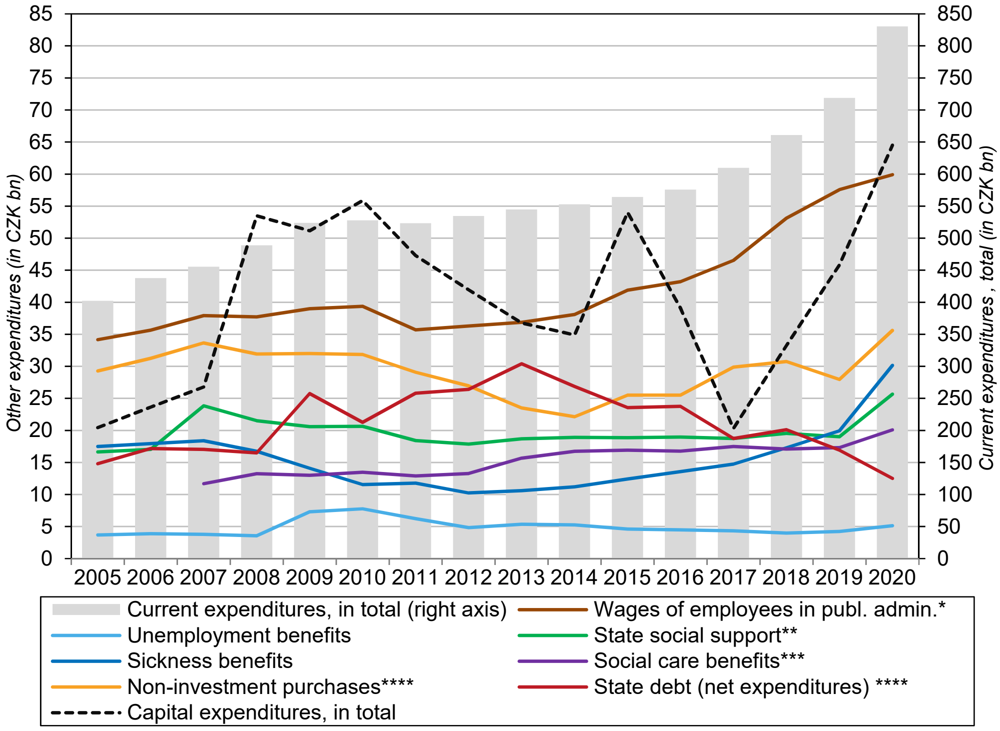
year-on-year. It was mainly thanks to the inflow of funds from the structural funds (+21.7 bn) as well as the cohesion funds (+5.1 bn). On the contrary, direct payments in agriculture, which formed one quarter of total revenues from the EU this year (from 82.1 bn), flowed undisturbed.

Size of the state debt accelerated during H1. Volume of issued state bonds overtook half a trillion CZK.

Value of the state debt accelerated in Q2 2020. At its end, its value was 2 157 CZK bn, quarter-on-quarter increase then 384 bn. The debt expanded by one quarter year-on-year and neared the record pace from Q3 of the crisis year 2009. To cover this year´s exceptional SB deficit, planned debt instalments (concentrated especially to the second half of year 2020) as well as strengthening liquid reserves, a record volume of state bonds (533 CZK bn)[68] was issued during H1. Similarly to the previous years, the borrowing activity was limited to the domestic market. Koruna value of the external debt thus further shrank (by 7% year-on-year). At the end of June 2020, the external debt constituted already less than one tenth of the total state debt (minimum in the last sixteen years). Financial institutions with 61% share remain the key holder of the domestic state bonds, non-residents owned 35% of bonds. In Q2 2020, position of financial institutions strengthened, and the weight of non-residents was one of the weakest since the end of year 2016 (when the CNB forex interventions were still in place). Net SB outlays to service the state debt[69] were 12.5 CZK bn in H1 and decreased by one quarter year-on-year.

Among holders of domestic bonds, the weight of financial institutions increased to the detriment of non-residents.

Chart 17 Selected expenditures of the state budget in accumulation for H1 (in CZK bn)



*Covers expenditures on salaries in central government institutions. Does not include e.g. wage costs of regional education.
**Also includes the foster care benefits.
***Includes Material deprivation assistance benefits, Benefits for people with disabilities, Care benefits based on Act on State Social Support.
****Contains mainly expenditures on purchase of services, materials, energies or other services (e.g. expenditures on repairs and maintenance).
*****Corresponds to the balance of the budget chapter State debt.
Source: MF CR, MLS

Indebtedness rate of the government institution sector so far increased only slowly compared to

Consolidated debt of the government institution sector was 1 894 CZK bn at the end of Q1 2020[70] based on the CZSO data. It strengthened by 3.2% year-on-year, and in comparison to the end of the last year even by 8.9%. More significant quarter-on-quarter growth of debt at the

[68] Their average annual yield was 1.15%, average maturity then 5.5 years.
[69] Corresponds to the balance of the budget chapter State debt (no.396). It consists of net interest outlays and also fees.
[70] Preliminary data regarding the debt and deficit of the sector of government institutions for Q2 2020 will be published by CZSO on 5th October, by Eurostat at the end of October 2020.

the long-term minimum from the end of year 2019. Budget balance however already deepened more.

year beginning was however apparent also in the previous three years. Indebtedness rate equalled 32.8% of GDP in Q1 and since the end of the last year, when it arrived at ten year minimum, increased by 2.6 p.p. Even though the domestic economy was only on the threshold of recession in Q1, budget deficit of government institutions already tested a boundary of 2% of GDP, which was the worst result since the end of 2014. It was connected with a fact, that a year-on-year decrease of total revenues of the sector (by 1.5%) occurred after more than three years due to the weaker collection of weight significant taxes. Dynamics of total outlays however remained high (+9.8%).

Budget deficit of government institutions in the EU countries increased to -2.3% of GDP at the beginning of the year.

Worsening of the condition of public finances was apparent in the vast majority of the EU states. Seasonally adjusted budget balance decreased by 1.6 p.p. to –2.3% of GDP quarter-on-quarter in Q1 2020, that is to the lowest level since the end of year 2014. Only Germany, Netherlands and Luxembourg kept a mild surplus (up to 1% of GDP) from the monitored countries[71]. Total nominal revenues of the government sector shrank year-on-year in half of the Union states. For outlays it concerned only Cyprus and their growth rate even strengthened in the half of states compared to the beginning of the last year (especially in countries of central and eastern Europe). The indebtedness rate in the EU continued in the descending tendency despite slowing growth of the economy for the most part of the last year. Turning point occurred already at the end of year 2020, when the indebtedness strengthened by 1.8 p.p. quarter-on-quarter (the most after year 2010) to the level of 79.5% of GDP. Negative development was more evident in the euro area countries (+2.2 p.p.), however 90% of Union states experienced at least a mild worsening. The indebtedness increased in 10 countries year-on-year – the most in Finland (+4.7 p.p.) and Romania (+3.6 p.p.), states strongly afflicted by the coronavirus epidemic (Spain, Italy, France, Belgium) were also included. In the CR, similarly to majority of its neighbours, the indebtedness mildly decreased. The CR thus held position of the fourth least indebted Union economy.

Quarter-on-quarter growth of the indebtedness rate reached ten year maximum in the EU in Q1. Worse position of states with fast outbreak of the covid-19 infection had an effect among other things.

[71] It concerns 21 countries providing seasonally adjusted data. Non adjusted data suggest that only four states achieved surplus. The balance worsened in the whole EU (apart from Cyprus) compared to Q1 2019. Belgium, Italy, Malta, Romania and France had the deepest deficit (over 9% of GDP) this year.