

7. Monetary Conditions

The Czech economy revived without a credit expansion in 2014

Even though the Czech economy again returned to growth in 2014, it was not financed by debt in such an extent as usual. Only in the last three months of 2014, the year-on-year rates of growth of credit to companies were above the year average (+3.1 %). The households however incurred debts below the year's average (+3.4 %) in the last quarter. Rate of growth of domestic credit (+4.1 %) was thus mostly under the direction of the government sector, especially then the central government – net credit to the government sector increased by 10.2 % year-on-year, credit to the central government (state) by 12.1 %.

Easing of monetary conditions persists

Money supply in the CR economy (M2 aggregate) rose by 4.6 % to CZK 3 429.9 bn in 2014 compared to 2013, that is slightly faster than the nominal GDP growth (+4.4 %). Expansivity of the monetary conditions was thus in this sense relatively small – apparent only in the first and the last quarter, the GDP in current prices grew compared to the additions to money supply faster year-on-year in the last two quarters. Still very low interest rates in the economy had a positive effect on the growth of the Czech economy and as the level of the koruna exchange rate affected by the CNB forex intervention had – koruna fluctuated against euro in monthly averages between values 27.39-27.82 CZK/EUR during 2014, between 25.48-25.95 CZK/EUR in 2013 (from January to October).

Term deposits of both firms and households (deposits with maturity and notice period) markedly shrank in 2014 (-108.1 bn crowns year-on-year, i.e. -12.6%) in the largest drop since 2010; it was a third year of continuous lowering of these deposits in a row

Both people and firms withdraw from their term deposits (deposits on accounts with maturity and notice period) and the speed of reduction of these deposits is accelerating (-5.1%, -4.9 % and -12.6 % in years 2012, 2013 and 2014). The main motive are apparently the low interest rates deterring from longer period savings, since the one day deposits on the contrary start to rise considerably (by +9.6 %, +8.3 % and +12.5 % year-on-year in the three mentioned years).

The behaviour of Czech households thus mostly had the decisive impact in 2014 on the fact, that deposits in the economy (quasi money) fell towards the end of the year compared to the same period of 2013. It was their second largest fall year-on-year in the time series starting 2002 – the largest reduction was recorded in 2010, this one was however characterised by a very bad situation on the labour market following the preceding crisis. They were lower by 2 % year-on-year in 2013.

High accumulation of funds on the current accounts of companies explains their strong investment activity, which was financed only to a lesser extent by credit

On the contrary, the non-term (one day) deposits – featuring considerably higher liquidity compared to terms deposits – further grew (+12.5 % year-on-year), especially on the giro accounts of households (+13.3 %). Strong accumulation of funds however continues on the current accounts of companies (+11.2 %), when these one day deposits of companies grow by double-digit rates already for the third year in a row. It can be assumed, that these funds represent – apart from usual operation financing – also a significant potential for future investment. Nearly five percent (+4.6 %) year-on-year addition to fixed investment in the Czech economy in 2014, which was the largest for the last seven years, could thus be on the part of companies financed just from the funds accumulated on the current accounts. It likely explains the strong investment activity without any significant indebtedness.

Still, as apparent from the development in Q4, the situation has been likely „returning to normal“, since the rate of growth of the corporate credit accelerated in this quarter and on the opposite the deposits on current accounts of companies grew significantly (CZK +86 bn). Especially the exporters experienced an inflow of additional profits practically during the whole year 2014 as a result of the koruna depreciation following the CNB forex intervention, which the companies likely cumulated on their current accounts (the balances on the current accounts were however lowering in the first half of the year, in times of shareholders' meetings, where the decisions were taken regarding the profit distribution and also their repatriation in firms under foreign control).

Consumer loans and housing loans increased in total identically year-on-year as in 2013, however the volume of consumer

People keep borrowing from banks, however only with caution. It follows from the bank statistics, that the aggregate credit to population for housing together with consumption credit increased (+4.4 %) by roughly the same rate as in 2013 year-on-year (+4.3 %) to 1.093 tril. crowns. However, while the housing credit rose due



loans decreased ...

to the favourable interest rates and due to anticipation of higher prices of flats in the future by 47.7 bn crowns (i.e. +5.6 %), the volume of consumption credit shrank by one percentage (-1.9 bn crowns).

...while keeping relatively significant share of non-performing loans on total credit to households for consumption

At the same time, the percentage of credit in default remains relatively high for credit on consumption (12.1 % of these loans against 12.2 % in 2013). Bank clients experience difficulties especially with not repaying their debit balances on the giro accounts (9.9 % in default in 2013 and 12.7 % in 2014) and also on the credit cards. Both these products are the most expensive from the view of interest rates charged by the banks.

The proportion of non-performing loans of companies is the lowest for the last five years and proves good financial health of firms strengthened also by the additional profits of exporters brought about by the depreciated koruna

Non-performing loans of non-financial businesses in relation to total credit of this institutional sector arrived at only 6.6 % towards the end of year 2014, which was the least since 2009. Risk lowered also year-on-year (7.2 % at the end of 2013, falling down from its half year). The proportion of non-performing loans of non-financial businesses does not need to present a problem with respect to the relatively good condition of the Czech economy, accumulated profits and so far adequate domestic as well as foreign demand.

Only the segment of entrepreneurs (households-trades), which owed less by 4 % by the end of the year 2014 year-on-year – the volume of their credit however already increased negligibly in 2013 (+ 0.9 %) - shows a relatively large share of non-performing loans for already four years. It was 12.7 % out of total provided credit by the end of 2014, which is roughly the average of the last four years (13 %). It confirms the generally known fact, that the segment of small and medium enterprises is generally more risky for the creditors in the economy.

The already very low deposit interest rates of banks further declined...

Interest rates on non-term deposits fall in case of new deals continuously already a fourth year in a row – it is from 0.72 % p.a. for giro accounts of households towards the end of year 2011 to 0.31 % in December 2014 (from 0.35 % to 0.15 % for firms). The rates of term deposits are also lower year-on-year (from 1.65 % to 1.4 % total deposits with maturity for households, the decrease for firms was less perceptible, at very low levels, i.e. from 0.31 % to 0.29 %). Deposit interest rates are not attractive and people likely search for saving alternatives to saving in banks – the value of their property in funds as well as the pension insurance grows. Direct investments into foreign stock recorded large yields in the past year.

... only the rates for mortgages became cheaper among the lent funds

Consumer loans did not become cheaper to the same extent as the credit for housing real estate acquiring. The rates remained at 14 % (compared to 14.1 % towards the end of 2013), rates of housing credit fell from 3.4 % to 2.9 %). With respect to companies, the difference in the price of the borrowed funds was only negligible (from 2.45 % by the end of 2013 to 2.22 % at the end of 2014, from 2.95 % to 2.9 % for an overdraft).

Chart 17 Credit dynamics (y/y in %)

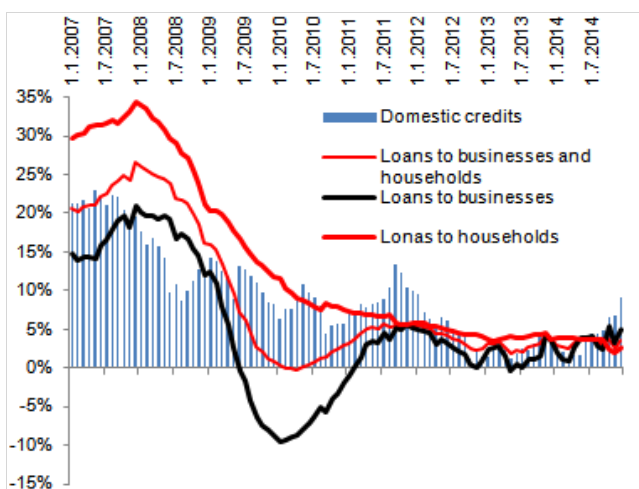
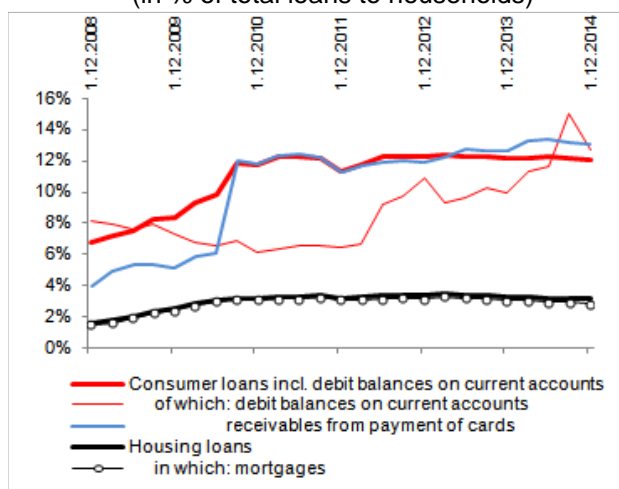


Chart 18 Non-performing loans to households (in % of total loans to households)



Source: CNB