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First half of 2019

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Latest information provided in this report has been dated the 6th September 2019.

1. Summary

- The Gross domestic product (GDP) rose by 2.7% year-on-year in both quarters of year 2019[1]. The consumption of households and government institutions still contributed the most to the growth. In contrast, the effect of the capital expenditure weakened. The foreign trade balance was positively reflected in the GDP growth especially in Q2. Improvement of surplus was rather caused by the slowdown of import, since the situation was worsening in foreign economies. The GDP growth was slackening in most EU countries, Germany even experienced a quarter-on-quarter fall. Domestic quarter-on-quarter GDP growth attained 0.7% in Q2.
- The Gross value added (GVA) increased by 2.8% year-on-year in Q2. The services branch contributed to the growth by a vast majority (2.3 p.p.), benefiting from the strong domestic demand. The GVA grew relatively strongly in the trade, transportation, accommodation and food service (3.8%). Information and communication also maintained a fast growth (8.9%). Manufacturing, the traditional driver of the Czech economic growth, on the contrary lagged behind. Its GVA increased by 1.2% year-on-year and its contribution to the growth comprised 0.3 p.p. Construction built on the last year with the GVA growth of 3.6%.
- Value of exported goods increased by 63.0 CZK bn (3.5%) year-on-year in H1 2019. The growth was caused mostly by the export of motor vehicles (+17.5 CZK bn) and computers, electronic and optical products (+10.2 bn). Value of imported goods enlarged by 45.4 CZK bn (2.6%) in H1. The resulting balance of trade with goods thus ended in surplus of 108.6 CZK bn, by 17.7 bn more compared to the same period of the last year.
- The total price level gauged by the GDP deflator increased by 3.5% year-on-year in Q2, representing the highest value since Q1 2009. Prices of consumption goods grew especially fast (3.8%), prices of capital goods then to a lesser extent (2.6%). Consumer price index increased by 2.8% year-on-year in Q2. Acceleration of the year-on-year growth of prices in the section of housing, water, energies and fuels continued. Food and non-alcoholic beverages also substantially contributed to the rise in the price level. Dynamics of the growth of prices of agricultural producers also strongly accelerated year-on-year to 11.0%.
- Year-on-year growth of the total employment[2] slowed to 0.8% in Q2. Employment remained unchanged compared to the preceding quarter. Services represented the cornerstone of the year-on-year growth of employment. Mainly the information and communication activities continued in dynamical development. Branches with the predominance of the sector of government institution, especially health and social care, also recorded an increase. The general unemployment rate was not falling significantly in Q2 and remained around the level of 2%. Year-on-year growth of the average gross nominal monthly wage of employees went down to 7.2% in Q2. The average wage thus climbed closely above 34 thousand CZK. In real terms, the average wage rose by 4.3%. The year-on-year dynamics was impacted by the swift growth of earnings in education, but also the slowing pace in manufacturing.
- The basic monetary policy-relevant interest rates were again raised in Q2. Client accounts had their conditions changed – interest rates mildly grew. Growth of the volume of the credit provided to households slowed down – for the consumer credit as well as mortgages. Even though the interest rates on credit were decreasing. Development of volume of credit provided to businesses copied the whole economy – growth markedly slackened in manufacturing, strong pace was maintained in case of information and communication.
- The state budget attained (based on the cash fulfilment) a deficit in the amount of 20.7 CZK bn within H1. The balance reflected a fast growth of some current outlays as well as investment activity. The growth of current outlays was markedly affected by the higher expenditure on social benefits year-on-year (+22 CZK bn, mostly the pensions) and by the wages in the regional education system (+13.7 bn). The investment activity also remained strong (+12.5 CZK bn). On the contrary, the state budget revenues grew

[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.

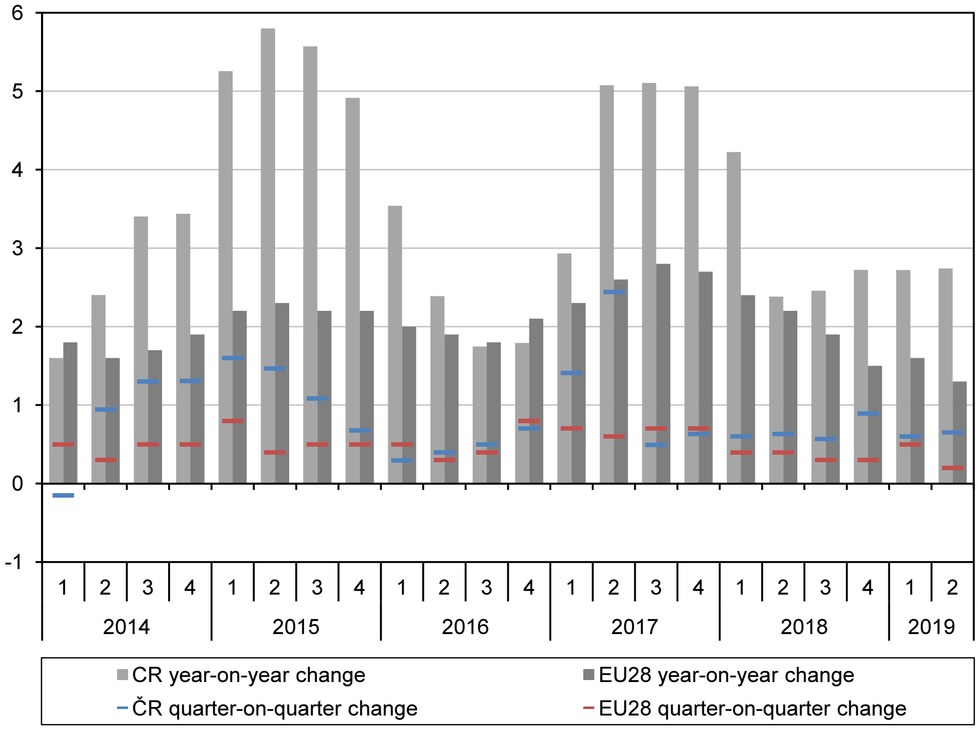
year-on-year less than in the previous years. Revenue growth was for the most part driven by higher incomes from taxes (incl. insurance) – the collection of VAT increased by 3.0%, income tax of natural persons from dependent activities by 13.3%. Non-tax and capital revenues also exerted a positive effect. State debt reached 1 712.6 CZK bn at the end of June and remained stable year-on-year.

2. Overall Economic Performance

Year-on-year GDP growth did not decline in Q2.

The year-on-year dynamics of the gross domestic product (GDP) was the same in Q2 as in the preceding quarter and reached 2.7%[3]. GDP growth in the CR thus does not follow the declining trend in many EU economies for now and remains at a stable level. Even though the expectations captured in the business cycle surveys signal cooling of both entrepreneur and consumer confidence for already several quarters. Breaking down the growth on contributions of individual components shows, that final consumption expenditures maintained their dominant role (1.8 p.p.[4]) in Q2, joined by the foreign trade balance (1.1 p.p.). In contrast, the capital expenditures dampened the year-on-year GDP dynamics (-0.2 p.p.) for the first time since Q1 2017. Compared to the previous quarter, the GDP increased by 0.7% in Q2, which confirmed the continuation of trend of moderate, but stable dynamics (GDP grew by 0.6% quarter-on-quarter in Q1). The gross value added (GVA) increased by 2.8% year-on-year in Q2. The services branches contributed the most similarly to the previous six quarters, prospering from the strong domestic demand. In the opposite direction, the contribution of manufacturing, which felt more the impact of slowing European economies, remained weak. Quarter-on-quarter addition of GVA reached 0.7% in Q2.

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



Source: CZSO, Eurostat

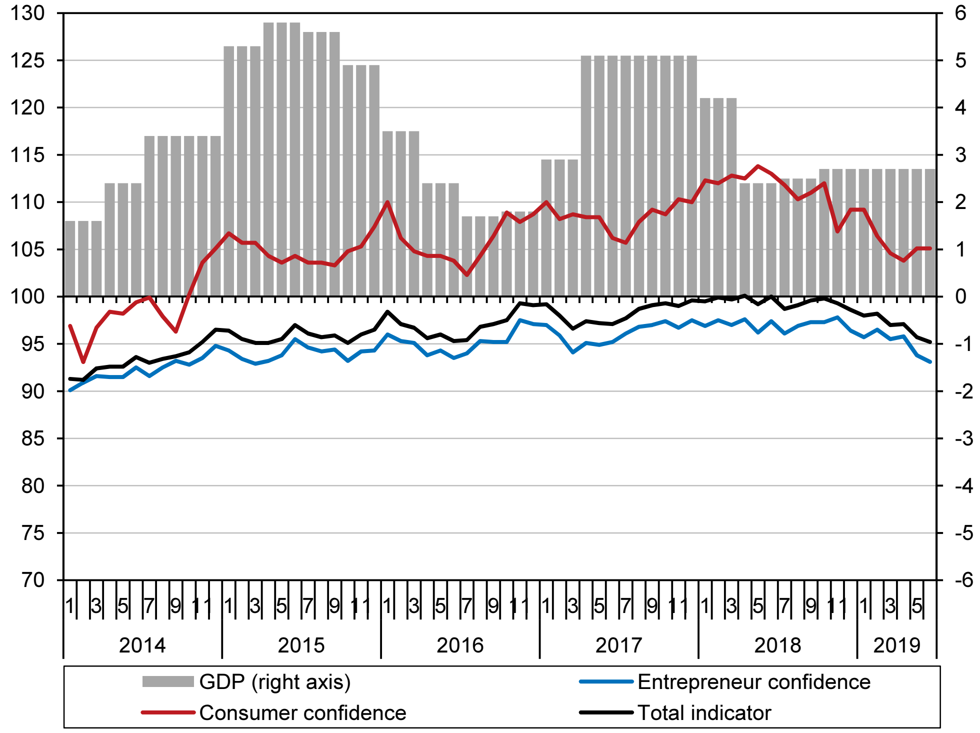
Growth slowed in many EU countries.

Year-on-year GDP dynamics again slowed in the European twenty-eight and arrived at 1.3%[5] in Q2. Quarter-on-quarter addition was also markedly lower (0.2%)

[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 30th August 2019.
[4] Additions to the GDP change after exclusion of imports for final use.
[5] Data for Bulgaria, Ireland, Greece, Cyprus, Luxembourg and Malta not available. Data for Slovakia are not adjusted for calendar effects.

compared to the previous period. The year-on-year growth of the largest European economy – Germany – slowed also in Q2 (from 0.9% in Q1 to 0.4% in Q2). GDP decreased by 0.1% here in comparison to the preceding quarter. Most EU countries registered a slowdown of the year-on-year dynamics. The most markedly in Croatia (from 3.8% to 2.5%), in Slovakia (from 3.4% to 2.5%) and in Slovenia (from 3.5% to 2.6%). Hungary (5.2%, the same as in Q1), Romania (4.6%) and Poland (4.2%) enjoyed the highest year-on-year GDP growth according to the available data. In contrast, Italy recorded year-on-year decline (-0.1%), the already mentioned Germany had the smallest addition and the GDP of the Great Britain, Belgium and Finland grew at the same rate of 1.2%.

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



Source: CZSO

Domestic demand was the main driver of the GDP growth.

Year-on-year growth of the final consumption expenditures was 2.9%. Households kept the dynamics from the previous quarter (2.7%). In case of government institutions, the year-on-year growth strengthened to 3.4%. Consumption of government institutions thus again notably contributed to the GDP growth (0.7 p.p.) in Q2. Quarter-on-quarter growth of household consumption reached 0.7%, it was 1.2% for government institutions. With the view to the durability of the consumed goods, further slowdown of year-on-year dynamics can be observed for durable goods in Q2 (3.0%[6]). And vice versa, the growth remained relatively high (6.6%) for the goods of medium-term consumption. The growth of consumption of non-durable goods stayed at a low level (1.8%). Year-on-year dynamics of consumption of services sank substantially – from more than 3% to 1.6% in Q2.

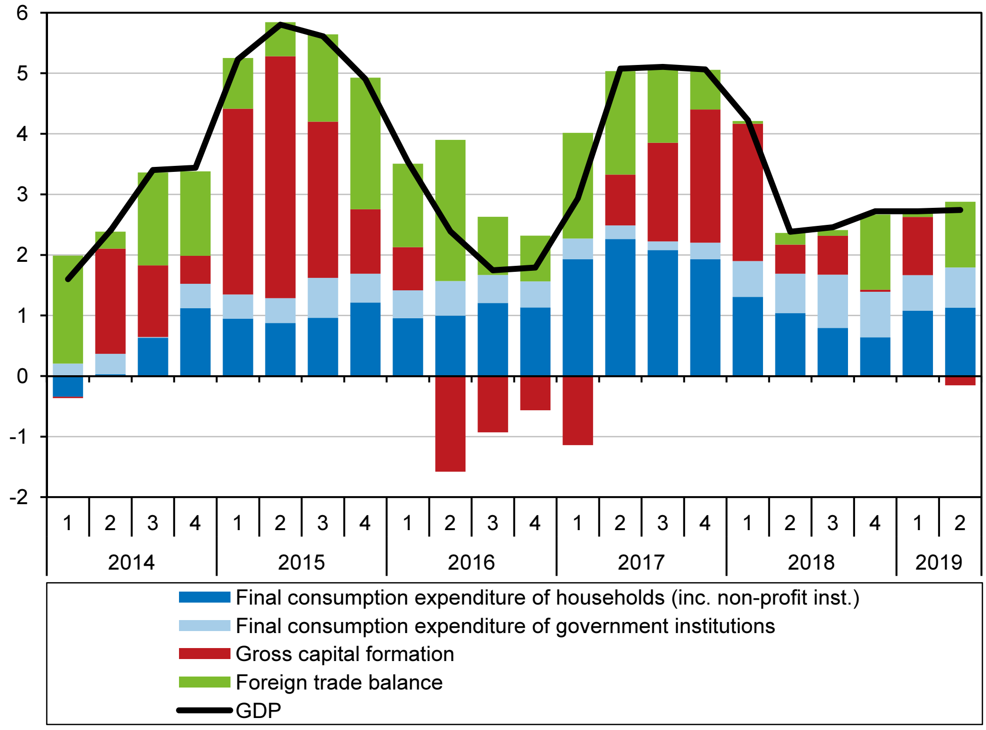
Volume of paid out wages and salaries increased by 7.5% year-on-year.

Volume of paid out salaries and wages grew by 7.5% year-on-year in Q2. It is by 0.4 p.p. less compared to the previous quarter. Volume of wage resources also did not expand as fast as in the last two years. Still, it presents a relatively strong growth, which is for the most part transferred into the size of wages themselves, because the

[6] Data related to consumption according to durability are in the domestic conception and not seasonally adjusted.

year-on-year increase of employment[7] was 0.8% in Q2, the least since Q3 2014. The price growth nevertheless strengthened in contrast to the previous years. The earnings thus grew by 4.4%[8] in real terms. The volume of paid out wages grew the most year-on-year in the area of real estate activities (15.1%) in Q2. Simultaneously, the employment fell here year-on-year by 0.8%. More than ten percent increase was in the group of branches public administration and defence, education, health and social work (10.6%). A relatively strong increase of total employment (2.1%) was also apparent in this group. Moderate slowdown of the dynamics, occurring since the last year, continued in case of manufacturing. The volume of paid out wages expanded here by 5.7% in Q2, accompanied by below-average growth of employment of 0.6%. Even though the total year-on-year rate of growth of employment was falling in the economy, it did not apply to information and communication, where employment grew the most year-on-year in Q2, specifically by 2.9%. Growth of the paid out wages in the given branch thus reached 7.9%, despite information and communication belonging to branches with the lowest wage dynamics.

Chart 3 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 imports for final use

Investment activity stagnated in Q2.

Expenditures on gross capital formation increased by 0.2% year-on-year in Q2, the least since Q1 2017. The expenditures on fixed capital formation themselves grew only slightly more (0.9%). Even this addition was however saturated by import, as shown by the comparison of contributions to the year-on-year growth of GDP. While without the exclusion of import the contribution of capital expenditures is zero, it already dampens the GDP dynamics by 0.2 p.p. after exclusion. Capital expenditures contracted by 5.6% compared to Q1. Type classification of gross fixed capital formation indicates, that the investment activity was cooling in all areas[9]. Expenditures on the intellectual property increased the most (3.3%), nevertheless it represents a substantial slowdown compared to the preceding quarter (9.3%) as well

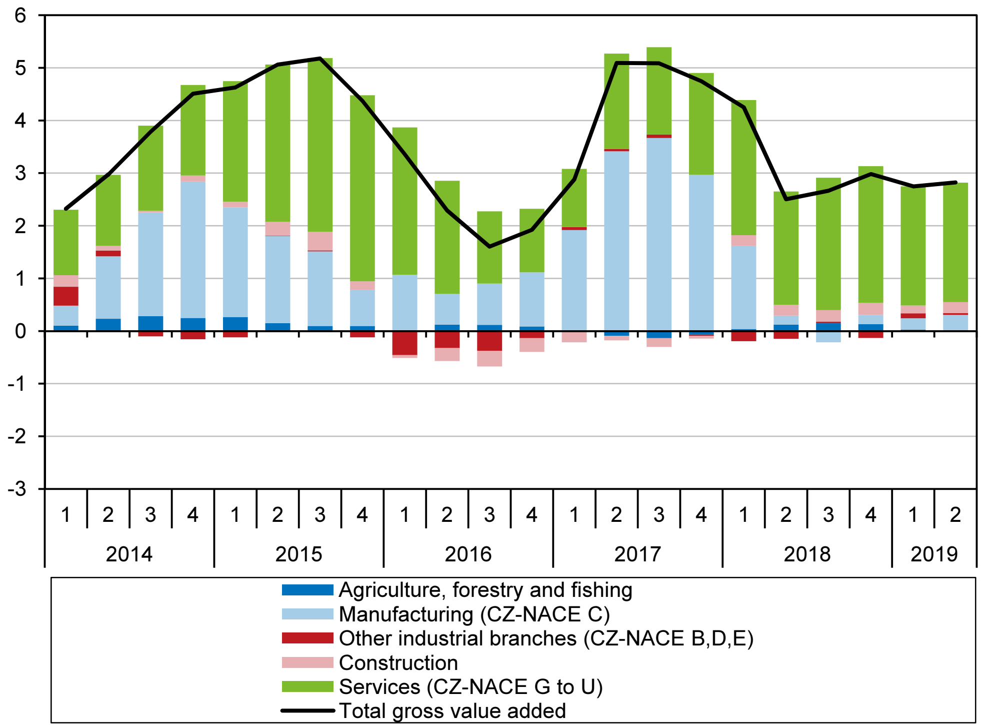
[7] Employment in the national accounts conception, figure seasonally adjusted.
[8] Converted into the real expression using the deflator of final consumption expenditure of households.
[9] Data regarding the type classification of gross fixed capital formation are not seasonally adjusted.

as year 2018 (5.2%). Year-on-year growth of investment into housing was 1.1% in Q2 and it was the lowest since the end of year 2017. Expenditures on other buildings and structures grew only by 0.2%. Other areas recorded a decrease. Investment into transport equipment was affected mainly by the last year´s high comparative basis (fall by 2.0% in Q2, growth by 13.0% in year 2018). The most weight significant expenditures on ICT and other machinery and equipment fell by 0.6% after eight quarters of year-on-year growth.

Foreign trade balance surplus expanded thanks to services year-on-year.

Surplus of the foreign trade with goods and services[10] attained 101.3 CZK bn in Q2 and expanded by 13.9 bn year-on-year. The given value is the highest in the whole time series available since year 1995 and the year-on-year addition is the strongest since Q3 2016. The trade with goods played the main role in the year-on-year improvement of the balance with the positive result of 68.5 CZK bn (year-on-year increase of 11.6 bn). Surplus of trade with services also increased (by 2.3 bn to 32.9 CZK bn). The change in foreign trade dynamics caused the vigorous growth of surplus, which became evident in Q2. The year-on-year rate of growth of exports in real terms (2.2%) overtook imports after six quarters (1.4%).

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



Source: CZSO

Services persisted on the position of the driver of gross value added growth.

The branches of the services sector play a dominant role in the year-on-year growth of the gross value added already five quarters, benefiting from the strong demand. On the other hand, the traditional driver of the Czech economic growth, manufacturing, experiences a decline. It is the effect of the weaker foreign demand. Trend of this nature continued also in Q2. Year-on-year addition of GVA of manufacturing amounted to 1.2% in Q2 and contribution to total growth reached 0.3 p.p. Branches of the services sector in total contributed to the GVA growth 2.3 p.p. Group trade, transportation, accommodation and food service featured the strongest contribution (0.7 p.p., 3.8%). Information and communication activities kept a brisk growth (8.9%),

[10] According to the methodology of quarterly national accounts (import and export in FOB/FOB prices).

which also assisted to relatively high contribution of this branch to the GVA growth (0.5 p.p.). Branches professional, scientific, technical and administrative activities (GVA growth of 4.4%) and also branches with the predominant public sector[11] (1.7%) supported the growth similarly by 0.3 p.p. Construction continued in the year-on-year growth of the GVA (3.6%), the branch contributed with a view to its relatively small weight to total dynamics 0.2 p.p.

3. Branches Performance

Year-on-year growth of the gross value added stayed mildly below the 3% level during H1. The economy has not slowed down also in the quarter-on-quarter expression so far.

Performance of all branches of the economy captured via the created gross value added (GVA)[12] rose by 2.8% year-on-year in H1 and thus repeated the result from the second half of the last year. Rate of growth was practically the same in this year´s Q1 and Q2. The quarter-on-quarter dynamics of GVA also remains stable, specifically already since the half of year 2017 (on average it was 0.7%, similarly to Q2 2019). Mainly this year´s result sounded positive for the domestic economy, especially in the context of less favourable external factors (notable slowdown of the economic growth in key export territories, further strengthened by the growing regulative measures in the international trade as well as the persisting uncertainty regarding the future organisation of relations between the Great Britain and the EU).

The focal point of the GVA growth was located in services already second year in a row. Here, the dynamical development of information and communication continued. Trade also prospered.

All eleven main branch groupings contributed to the year-on-year GVA growth this year. The tertiary sector presented the focal point of the growth similarly to the whole last year. Its performance strengthened by significant 3.7% in H1 2019 and managed to secure four fifth of the GVA growth of the whole economy on its own. Within the services primarily the information and communication grew (+8.7%), it increased its GVA by more than one half since the end of the last recession (year 2013). Weight significant group trade, transportation, accommodation and food service (+3.9%) also built on the strong last year, profiting from the growing purchasing power of households, expansion of the foreign trade with goods as well as the tourism. All other branches of services also fared well, especially the professional, scientific and technical and administrative activities (+4.4%, the strongest half-yearly pace since the first half of year 2016). Within services the group public administration and defence, education, health and social work featured the slowest growth of GVA (by 1.7%), its dynamics however did not defy the trends of the three preceding years.

GVA growth in manufacturing diminished to 1%. Together with H2 2018, it recorded the weakest rate of growth since the end of the last recession.

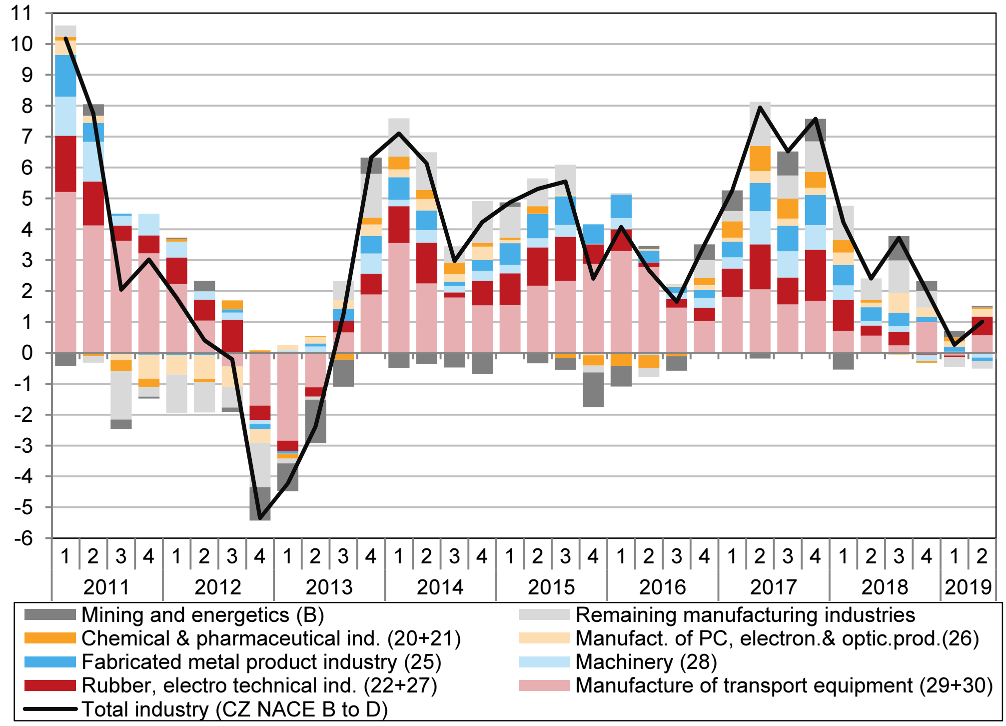
Connected to the development in Germany as well as the whole euro area[13], the slowdown of performance of the domestic manufacturing continued. GVA fell here by 0.1% in H2 2018 and was thus assigned the weakest year-on-year performance since the end of the last recession. It achieved only 1% growth in the subsequent half-year and quarter-on-quarter it on average only stagnated. Non-manufacturing industrial activities fared slightly better this year, specifically thanks to the development in energetics. Growth in construction continued in H1 following the last year´s turnaround (+3.1%), the branch performance however still mildly lagged behind the level from the business cycle peak in the last decade (by 2%). GVA grew by moderate 0.6% in the primary sector in H1. Higher volume of logging of bark beetle wood, mild increase of the production of meat as well as milk and further also the year-on-year growth of the sowing area as well as yields of the first harvested winter cereals[14] could have worked here in the direction of real output growth.

[11] Public administration and defence, education, health and social work.
[12] GVA data are expressed in constant prices and adjusted for seasonal and calendar effects.
[13] Growth of total value added in these groupings notably slowed already during the whole last year. It achieved weak 1.2% in the euro area countries in its last quarter, even 0.5% only in Germany. The similar rates fell to 1.1%, resp. 0.3% in Q2 2019, worse results were reached lastly in year 2013.
[14] According to the July CZSO harvest estimates, the production of the first harvested cereal (winter barley) increased by 21% year-on-year this year. The sowing area expanded by 5%, estimate of the per hectare yield was 5.74 t/ha (year-on-year +15%, +13% against the ten year average). Winter barely comprised below 8% of the total harvest of basic cereals in the CR last year. According to the operative report of the Ministry of Agriculture, 36% of this crop was harvested at the end of the first July week. Harvests started slightly later this year in comparison to the last year.

Domestic industry recorded repeated quarter-on-quarter drop of output on the turn of years 2018 and 2019. It thus with a lag reacted to the development in the euro area.

Business statistics proved a more detailed view of the constituent branches. It is not surprising with respect to the marked export orientation of the domestic industry[15] as well as the strong interconnection especially with the development in Germany[16], that its growth halted towards the end of the last year. Industrial production index[17] fell by 0.1% quarter-on-quarter in Q4 2018 and its fall further deepened to 1.0%[18] in the subsequent period. Industry thus recorded the weakest result since the end of year 2012. This development was gradually imprinted into the year-on-year dynamics – output grew only by 0.3% in Q1 2019, by 1.0% in Q2. Some domestic factors also did not ease the situation for the industrial businesses in the CR (lack of qualified workers and associated higher wage costs, rising prices of energies).

Chart 5 Contributions of sub-branches to the year-on-year change of the industrial production (in percentage points, adjusted for calendar effects)



Source: CZSO

Manufacture of electrical equipment and also energetics contributed the most to the growth of the total industrial production.

Long-term expansion of manufacture of computers, electronic

Despite less favourable development of the foreign demand, the majority of industrial sub-branches also experienced at least a mild year-on-year growth of output in H1. Manufacture of electrical equipment (by 0.3 p.p., growth of the branch by 4.4%) contributed the most to the increase of the total industrial output (by 0.6%), mainly due to the acceleration driven by the domestic demand in Q2. Contribution of the long-term growing but by weight peripheral pharmaceutical industry was also significant (0.2 p.p.), since its output enlarged by more than one sixth this year. Similarly the energetics and also manufacture of computer, electronic and optical products supported the whole industry, with the brisk growth (+6.2%) mirroring mostly the growing domestic demand. This branch also belongs to the fastest growing industrial fields

[15] Industrial businesses realised nearly 60% of their sales through direct export in the CR in H1 2019 (for some branches – manufacture of transport vehicles, electrical equipment or manufacturing of computers, electronic and optical equipment – it was three quarters, even over 80% in pharmaceutical or leather manufacturing). Further part of sales was also associated with the foreign demand and realised in the form of indirect exports.

[16] According to the national conception of the foreign trade, 31.4% of the whole goods export (comprised in overwhelming majority by industrial products) was directed to Germany in H1 2019, even 65.7% to euro area countries. Both shares remain relatively stable in the current decade.

[17] Includes branches of Mining and quarrying, Manufacturing and also Energetics (here assumed as a branch of manufacturing and distribution of electricity, gas, heat and air conditioning). All year-on-year rates of growth of output (at the level of both the branch sections and divisions) are adjusted for calendar effects, quarter-on-quarter rates are then also seasonally adjusted.

[18] Businesses thus reacted with a lag on the situation in the euro area, where the industrial production index in the quarter-on-quarter expression halted already at the beginning of year 2018 and also did not revive as the year progressed. On the contrary, the output decrease deepened in Q4 (to 1.1%) and featured a year-on-year fall as well for the first time since last recession period (by 1.9%). Lowering of output occurred simultaneously also in all five largest EU economies (year-on-year as well as quarter-on-quarter).

and optical products continued.

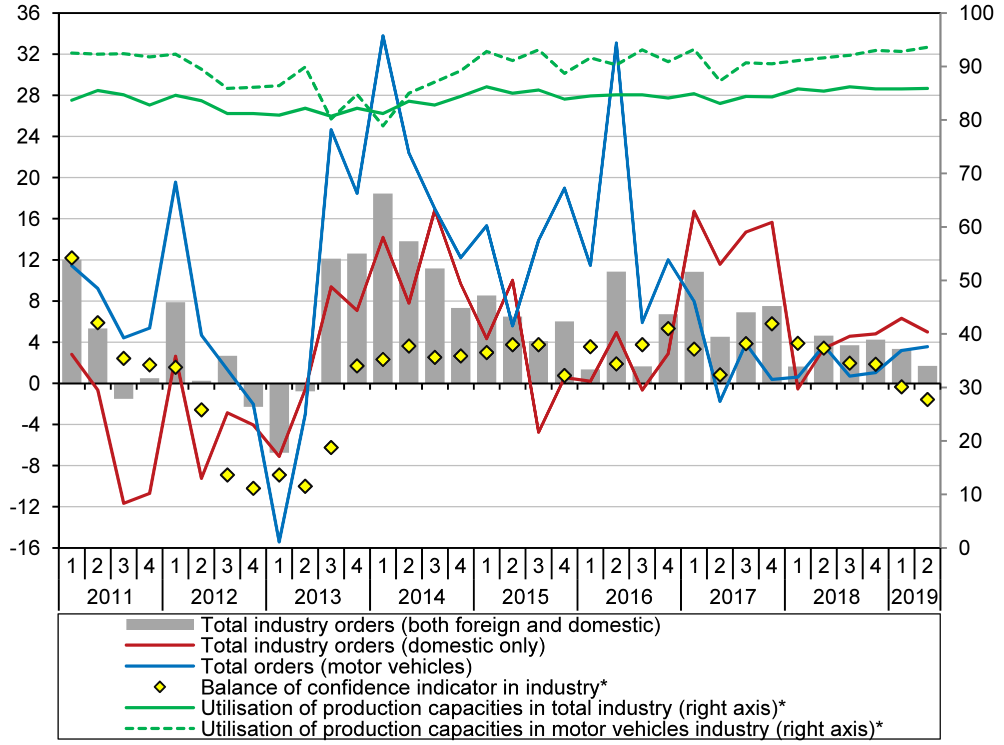
since the end of the last recession[19]. Output in the weight dominant branch of manufacturing of motor vehicles went up only by 0.7%, the least since year 2013. It was also evident from the data regarding the physical output[20]. New orders signalled a perceptible weakening of dynamics here already last year (the value of foreign orders increased by 2.5% for the whole last year, it fell by 1.2% for the domestic orders). Situation of manufacturers of other (especially rail) transport equipment improved this as well as last year. Output increased here (6.3%) mainly thanks to the foreign demand in H1 2019. Within the more significant branches by weight, the output moderately increased in repair and installation of machinery and equipment and also in the food industry – i.e. in activities primarily focused on the domestic market. Output stagnated in manufacture of rubber and plastic products or fabricated metals, despite lasting growth of the domestic demand it was slightly falling in machinery (–0.7%). Performance fell deeper in metallurgy and foundry industry (–2.8%), because the strong domestic demand from years 2017 and 2018 ceased. Manufacturing of other non-metal mineral products, where the strong growth impulse connected to the domestic demand for construction materials likely already evaporated, was in similar situation. Output also dropped in the chemical industry this year (–2.8%), mainly due to the irregularities in the usage of production capacities, which are typical for this field. Long-term downturn in mining and quarrying (by 4.4% this year, by 42% for the last fifteen years) concerned primarily coal[21].Output in the wood industry decreased by one tenth this year and thus returned to the level of the first half of year 2016. In spite of its low weight, this field worked against the growth of the whole industry the most in H1 2019 (addition –0.2 p.p.).

Motor vehicle manufacturers recorded the weakest growth since H1 2013.

Output mildly declined in machinery, deeper than in metallurgy, chemical and wood industry.

Long-term slump of the mining of coal lasted.

Chart 6 New orders in manufacture of motor vehicles, in industry in total (in current prices, year-on-year change in %), **balance of confidence indicator in industry*** (in points) **and utilisation of production capacities in industry*** (in %)



Source: CZSO *Data are seasonally adjusted

[19] In the last six years (resp. against H1 2013), the production here increased in total by 61%, only manufacture of motor vehicles recorded a faster pace (+70%). Growth arrived at 28% in total industry. Only energetics (–1%), wood industry (–4%), mining and quarrying (–18%) and manufacture of leather products (–23%) stayed below the level of year 2013.

[20] Based on data from the Automotive Industry Association, there was 747 thousand passenger cars manufactured in the CR in H1 2019, and the production by 1.5% lagged behind the last year´s record number. Manufacture of other parts and accessories for other types of motor vehicles (eg. busses) on the contrary mildly increased.

[21] In contrast in other, so far by weight peripheral segment of mining and quarrying activities – quarrying of building materials (especially stone, sand and clay) – production have grown briskly already third year in a row.

Rate of growth of domestic sales of industrial businesses exceeded the sales from direct export already third year in a row.

Despite weakening dynamics of production, the nominal sales of industrial businesses rose by 3.1% year-on-year in H1 2019 (nearly by 2 p.p. more than in the same period of the last year, when there was even one working day more). They thus clearly pointed to the upward movement of prices in the economy. Similarly to years 2017 and 2018, domestic sales grew faster (+3.8%) than sales from direct export this year. Total sales fell only in four industrial fields, given the more significant, it was the chemical industry (by 1.9%) and metallurgy (by 1.4%). On the other hand, they increased by more than one tenth e.g. in manufacture of leather or pharmaceutical industry and in energetics.

Value of new domestic orders year-on-year rose in Q2. It stagnated for foreign orders.

Balance of confidence indicator dropped to nearly six-year minimum, inadequate demand presented the again main barrier to growth after two years.

Prospects of the industry in the CR towards the second half of year 2019 remain full of contradictions. On one hand, the moderate growth of the value of new orders persists[22]. It reached 1.7%[23] year-on-year in Q2, if only thanks to the domestic orders (+5.0%). Further motor vehicle industry, incl. its closest sub-suppliers signalled a mild growth of demand. Significant branches – machinery, manufacture of metal products or chemical industry - were however in the opposite situation. Utilisation of current production capacities in whole industry remained high (86%). Seasonally adjusted balance of the confidence indicator in industry descended into the negative band after more than five years at the beginning of year 2019 and the subtle pessimism further deepened in Q2 (to –3.0 points in June). Given the main barriers to growth, weight increased for inadequate demand (from 33% in Q4 2018 to 40% at the beginning of Q3 2019) and the role of labour force shortage diminished (from 45% to 39%)[24]. Businesses also face more the lack of material since half of year 2018. One fifth of businesses on the other hand did not identify any significant barriers.

Growth of construction output grew already third year in a row. The warm weather had an effect as well as strengthening of public investment on infrastructure projects.

Growth of construction output[25] slackened this year following the strong last year, nevertheless it continued for the third year in a row. It attained 3.4%[26] year-on-year in H1, also assisted by a swift entrance into this year – output increased nearly by 4% quarter-on-quarter for the first three months, when the warmer weather also fuelled the faster take-off of construction works. Further positive effect also originated from higher public investments connected to the faster drawing on funds from the EU budget, as well as a gradual expansion of residential construction. Despite weaker dynamics (+2.6%), weight dominant building construction added to growth of total construction production approximately by one half more than civil engineering construction (+6.2%) in H1.

Brisk growth of volume of started residential construction continued already third year in a row. Number of flats in multi-dwelling buildings hit the highest value since the end of year 2008.

It is also evident from the building construction performance, that the residential construction is gaining strength, thus gradually reacting to the longstanding strong demand in this area. Number of started dwellings was by 15.4% year-on-year higher in H1. It recorded a notable growth for the same time period already third year in a row. This year´s construction volume (19.1 thousand flats) thus already notably approached the so far record value for the same part of the year 2008 (21.9 thousand). Year-on-year expansion of started dwellings manifested in all main types of construction apart from the peripheral segments of non-residential buildings and reconstructed non-residential premises[27]. The largest increase of flats occurred in multi-dwelling buildings (+59%), construction reached the eleven year maximum here (6.0 thousand flats). Even though in the regional view, Prague contributed the most to the year-on-year growth

[22] New orders are surveyed 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.

[23] July 2019 showed more favourable outlook, when new orders strengthened in total by one tenth year-on-year and by one sixth in the motor vehicle industry.

[24] Growth of registered number of employees of industrial businesses halted this year. It was by 0.5% lower year-on-year in Q2.

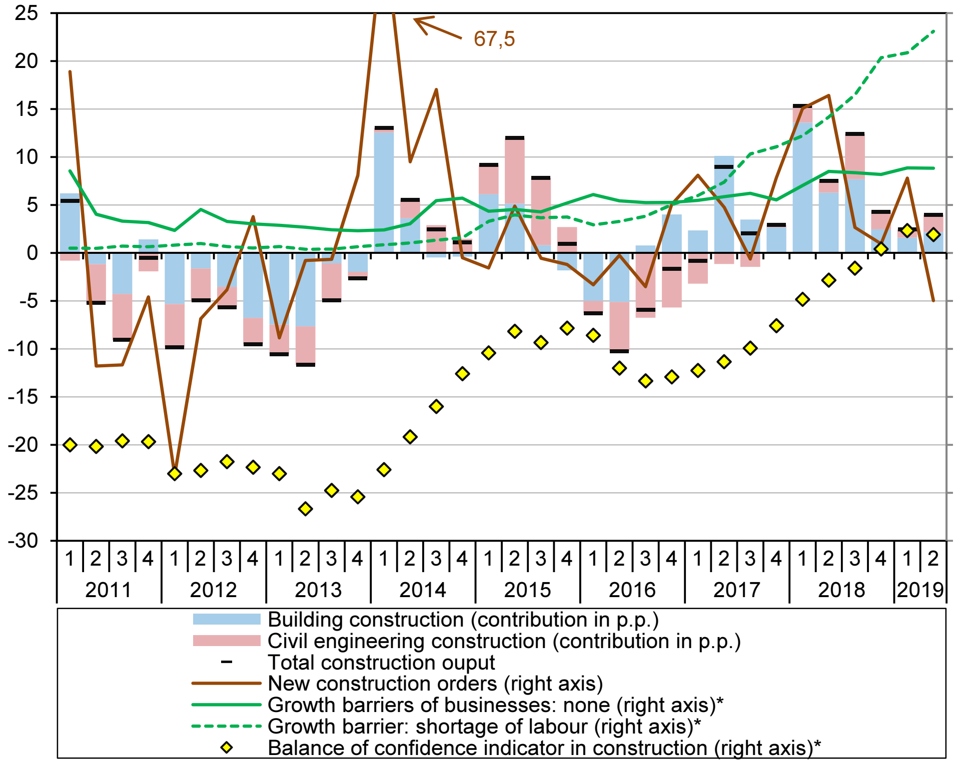
[25] All year-on-year data regarding the construction output are adjusted for calendar effects, quarter-on-quarter rates of growth also for the seasonality effect.

[26] Output growth followed a similar pace also in the whole EU. There, construction boom was under way in Romania (+23%) and especially in Hungary (+35%), where the steep growth lasted already three years in a row. Nearly all Union countries registered growth in H1, construction growth supported some economies balancing on the edge of recession, e.g. Germany (+3.8%) or Italy (+4.0%).

[27] „Popularity" of dwellings originating from reconstructed non-residential premises however grows in the last five years. 1 140 dwellings were created here for the whole last year, the most after year 2005. More than one half of these were located in Central Bohemia and Ustecky region in year 2018. Frequency of dwellings completed in the extensions to residential buildings also grows – 1 025 dwellings were completed this way in H1 2019, which presented the largest half-yearly sum after year 2006. It can constitute an interesting alternative with respect to time and finances to significantly predominating construction of new residential buildings especially in the largest cities.

in H1 and volume of commenced construction hit the four-year maximum here (2.5 thousand.), it still lagged behind the increase in population as well as job opportunities in Prague.

Chart 7 Contributions of branches to year-on-year change of construction output (in p.p.), **total construction output and new orders** (year-on-year in %), **balance of confidence indicator in construction*** (in points, right axis) **and selected barriers to growth*** (in %, right axis)



Note. Data Related to construction output are adjusted for calendar effects.
*Data are seasonally adjusted.
Source: CZSO

Growth of new construction orders due to the high last year´s basis halted in Q2. Total stock of work however expanded, mostly thanks to public orders.

Short-term prospects of construction remain positive, despite the fact, that the value of new domestic orders (for businesses with 50 employees and more) fell by one tenth year-on-year in Q2 2019 (by similar pace in both building and civil engineering construction). This development was however primarily affected by high comparative basis[28]. The volume of new construction orders stagnated during the whole half-year (given a mild growth in the civil engineering construction). Development and modernisations of transport infrastructure were also the cause for larger projects to eventuate, average size of new order grew third year in a row (to half-year 4.3 CZK mil[29]). Total stock of construction work also strengthened year-on-year (not yet realised orders) – by 7% to 184 CZK bn (according to the figure at the end of June). This was a result of the growth in public orders – they already comprised three fifths of the construction work reservoir (it had higher weight last in the first half of year 2010). Given the intense utilisation of construction firms[30] the role of foreign orders was on the other side falling, its stock failed to reach even one third of their level in year 2014. Value of confidence indicator in construction left the negative band in November 2018 (for the first time since September 2008) and it tightly exceeded the so far record optimism from year 2005 at the beginning of year 2019 (+5.5 points). The confidence did not grow in the further part of the year any more, but still

Entrepreneur sentiment in construction stayed mildly positive. Highly busy construction firms were however considerably troubled by a shortage of labour force.

[28] New orders hiked up to 71.3 CZK bn in Q2 2018. Their size as well as year-on-year pace (+33%) counted among the highest in the CR era.
[29] The approximate value per one building permit also increased (it was 4.7 CZK mil in H1 2019, 4.2 mil a year ago). It grew the fastest for new construction year-on-year (both residential and non-residential buildings). Total value of buildings permits strengthened by 19% year-on-year.
[30] Total stock of orders provided construction firms with work for on average further 10.5 months in Q2 („only" for 9.2 months in the same period of year 2018). Capacity of construction businesses in the CR is thus very stretched not only historically, but also in the international view. Within EU members, only businesses in Spain (16.8 months) and Italy (12.8) were busier this year. Slovakia (9.8) and Poland (9.6) also recorded high values.

remained mildly positive. The steep growth of businesses, whose development was limited by a shortage of labour force[31] on the other hand continued.

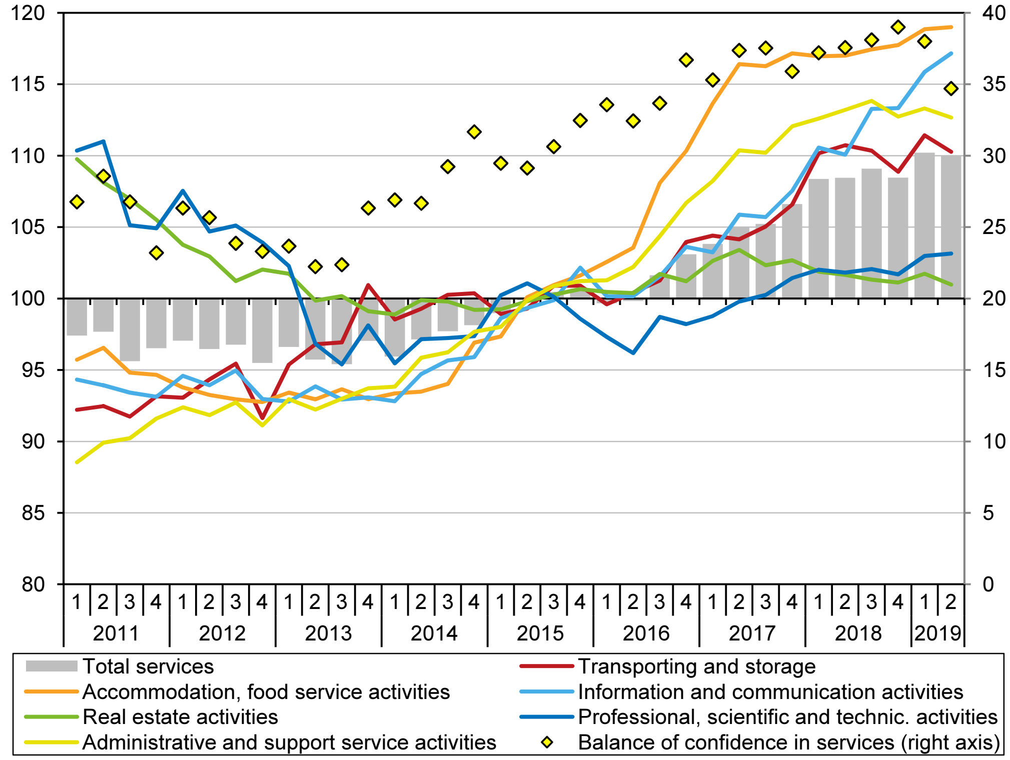
Sales growth in selected services moderated compared to last year, especially due to the effect of marked slowdown in transporting and storage.

Sales in selected services[32] rose by 2.0% year-on-year in H1 2019, the slowest pace after year 2016. Effect of the weaker Q2 was also felt this year, when the sales slightly dropped quarter-on-quarter (by 0.2%, mostly due to the slowed output in transporting and storage). All branch sections contributed at least to some extent to the year-on-year growth apart from the real estate activities, which lower sales in the segment of real estate agencies and real estate management[33] curbed.

Long-term strong demand for information and communication persisted.

Sales grew the most in the long-term dynamic branch of information and communication (+5.7%) this year. This branch added to the growth of all services sections from more than one half. Except for telecommunications (+2.6%), all sub-branches recorded a dynamic growth – the most the rather marginal segment by weight motion picture and music industry (+13.0%)[34]. Branch transporting and storage did not build on the strong output from the beginning of the last year, it showed only 0.5% sales growth in H1 of this year. Mainly weaker output in storage had an effect. Slowdown however occurred also in weight dominant land transport (to +1.7%), despite higher mobility of population supported by recorded employment as well as broader discounts in the public transport (for students as well as seniors aged 65 and more).

Chart 8 Sales in selected services divisions (in real terms, seasonally adjusted, level of year 2015 = 100) **and balance of confidence indicator in selected services*** (in points)



*Data are seasonally adjusted, include also the financial sector.
Source: CZSO

[31] If the inadequate demand troubled one half of construction businesses and shortage of workers one fifth of them in Q3 2017, these relations nearly turned two years later. Construction thus experienced a similar situation (in slightly accentuated form), which occurred in industry during years 2016 and 2017.
[32] Excluding trade, financial and insurance activities, research and development, and also public services. All data for services are in constant prices, year-on-year data are adjusted for calendar effects, quarter-on-quarter data are adjusted for seasonal effects (including the effect of the different number of working days).
[33] Sales in the more significant segment (by weight) “the sale and renting of real estate” remained stable year-on-year.
[34] The segment of motion picture distribution itself also thrived. According to the Union of motion picture distributors, the sales from entrance fees in cinemas in the CR increased by one quarter year-on-year and number of visitors reached 8.8 mil. in H1 2019 – the largest amount within first half-years in the history of independent CR.

Management consultancy, legal and accounting activities as well as market research prospered.

Growth of sales nearly ceased in administrative and support service activities.

Branch accommodation, food service and restaurants prospered (+2.3%), sales increased by 29%[35] here in the last five years. Sales dynamics corresponded to the development of number of overnight stays of guests in the collective tourist accommodation establishments[36]. Sales strengthened by 2.4% in branch professional, scientific and technical activities. Similarly to last year, they were pulled mainly by the legal and accounting activities and also rising demand for activities of head offices and management consultancy. Dynamic growth of sales for market research and public opinion polling continued by double-digit pace. On the other hand, sales for architectural and engineering activities grew only mildly (+1.3%) despite the expansion of construction. Branch administrative and support service activities grew by the weakest rate of growth after H1 2010 this year (+0.2%). Drop of sales of security and investigation activities, job agencies as well as travel agency activities was offset by a strong demand for office administrative and support activities and in the area of rental and operative leasing activities.

Brisk and relatively stable rate of growth of sales in retail trade persists already fifth year in a row.

Sales for trade of non-food goods in the CR climbed up by the fourth highest rate of growth among the EU states.

Growth of purchasing power of both wages and pensions together with the positive (even though slightly weaker) consumer confidence balance resulted in 5.2% year-on-year growth of sales in retail trade in H1[37]. The sales have maintained similar pace already for five years. Sale of non-food goods (with the growth of 8.0%, even 9.2% in Q1 2019) traditionally contributed the most to the year-on-year strengthening of retail in the CR. Its half-year growth more than doubled the rate of growth in the EU and among the Union states, only Lithuania (9.9%), Romania (9.7%) and Hungary (8.4%) recorded higher value. All types of specialised shops prospered, especially those with computer and communication equipment (+10.6%). Retail sale of cultural and recreation goods fared even better (11.5%), especially thanks to strong sales in Q1, which were stimulated by a fast onset of the Spring season. Only specialised shops with food experienced a moderate decline (by 1.2%). Total sales for food were however growing (+2.3%), similarly to the last year. On the contrary, the decreased dynamics concerned sale of automotive fuel, which increased year-on-year only by 2.2% (the least since the half of year 2014) in Q2 itself. Sales for sale and repair of motor vehicles continued falling similarly to the last year, however their fall already halted in the quarter-on-quarter expression this year.

4. External Relations

Value of export rose year-on-year in both quarters of year 2019.

Value of export of goods increased by 63.0 CZK bn (3.5%) to 1 878.4 bn[38] year-on-year in H1 2019. Export dynamics was even in individual quarters. While the export increased by 3.5% (31.8 CZK bn) year-on-year in Q1, Q2 did not fall much behind with 3.4% (31.3 bn). Value of export was 948.5 CZK bn in Q2 and was thus the highest reached for this period in the time series since year 2005.

Export outside the European Union featured stronger dynamics in H1.

Value of export of goods into the EU increased by 3.5% and by 4.7% outside of the EU year-on-year in H1. The dynamics was changing during the individual quarters – growth of export into the Union weakened to 2.6% in Q2 and export outside the EU on the contrary sharply accelerated to 8.0%. Year-on-year dynamics of export to Germany remained on moderate level in the first half of the year (2.4% in both Q1 and 2). However, Q2 was the one weaker for other EU countries. It was valid for Poland (slowdown from 3.1% to 0.8%), Slovakia (from 10.8% to 4.8%), Austria (from 6.0% to 2.0%) or France (from 9.4% to 1.1%). On the contrary, export to Hungary accelerated (to 9.4%) in Q2. Export to Belgium featured a year-on-year decrease (by 6.9% and 1.6% in individual quarters). Growth

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[35] It was the most among all branch sections of services. Growth arrived at 25% in information and communication.

[36] It grew by 2.5% year-on-year in H1 2019, for the most part thanks to domestic visitors (+4.0%). Visitors from Germany, other neighbouring countries of the CR and also from the USA contributed the most to the slight increase of number of overnight stays of non-residents. Decrease was on the contrary observed for visitors from Russia (visitors: –1.6%, overnight stays: –7.8%). All regions of the CR except for Zlinsky region (–1.2%) recorded an increase of overnight stays of visitors, rates of growth were weaker in Prague (+0.6%).

[37] All year-on-year rates of growth of retail sales are given in constant prices and adjusted for calendar effects, quarter-on-quarter rates are adjusted for seasonal effects (including the effect of different number of working days).

[38] Statistical data of the foreign trade in the national conception in the nominal terms including only the trade with goods. The value of exports is captured in the FOB prices, i.e. including the costs connected with the transport to the CR boundaries. Import depicted lower in this chapter is in CIF prices, i.e. including costs associated with the transportation abroad, up all the way to the CR boundaries. Data valid as of 6th September 2019.

detected towards the end of the last year and at the beginning of this year for export to Great Britain did not hold and export fell by 7.8% in Q2. Acceleration of year-on-year dynamics of export outside the Union was partially due to the comparative basis of the last year´s Q2. Nevertheless, the value of export to Russia (11.4%), United States (17.6%) and Switzerland (8.1%) grew relatively strong in Q2.

Export of motor vehicles revived in Q2.

Increase of the value of export of motor vehicles (+17.5 CZK bn, 3.4%) and also computers, electronic and optical products (+10.2 bn, 5.8%) supported the solid growth of export in H1. Increase of value of export of other transport equipment (+5.0 bn, 19.1%) and chemicals and chemical products (+4.4 bn, 5.3%) was also stronger. Export of two significant items – machinery and equipment (+5.1 bn, 2.5%) and electrical equipment (+2.2 bn, 1.4%) then featured a relatively weak dynamics. Growth of export of motor vehicles gained pace to 5.4% in Q2 itself and on the contrary the value of mentioned items tied to the manufacture of motor vehicles – machinery and equipment (0.2%), electrical products (0.5%) and also rubber and plastic products (0.9%) stagnated.

Import growth in contrast slowed in Q2. Import from the EU stagnated.

Year-on-year dynamics of import of goods stepped on the brakes compared to H2 2018. Value of import increased by 45.4 CZK bn (2.6%) in total to 1 769.8 bn in H1 2019. The deceleration however took place mostly in Q2 of the year. Value of import rose by 8.3 CZK bn (0.9%) year-on-year to 890.1 bn in this time period. Import grew nearly exclusively from countries outside the EU in H1 (7.6%), on the contrary only by 0.3% more was imported into the CR from the EU than in the same period of the last year. In Q2, the value of import from the EU even slumped by 1.2% year-on-year. It was caused mainly by the sinking import from Germany by 2.7%, slump of the import from Slovakia also deepened to 10.7% in Q2. Strong decline continued also in case of Great Britain (-9.9%). Among the destinations outside the EU, import increased especially from China (similarly by 9.0%) in both quarters of 2019. Import from South Korea (–9.0%), United States (–7.4%) and Russia (–20.2%, caused by the stopped supplies of oil due to its pollution) featured relatively strong decline year-on-year in Q2.

Import of motor vehicles increased only negligibly.

Value of import of motor vehicles grew only slowly in H1 (+5.4 CZK bn, 1.9%). Value of imported computers, electronic and optical products (+8.1 bn, 4.5%) attained the largest addition. Oil and natural gas recorded import increase of 6.9 CZK bn (12.0%). Import of chemicals and chemical products (4.9 bn, 3.5%), machinery and equipment (5.6 bn, 3.3%) and electrical appliances (2.8 CZK bn, 2.2%) slightly grew. However similarly to the export side, import of machinery and equipment (0.5%) as well as electrical products (0.4%) stagnated in Q2 itself. Value fell for imports of basic metals (–3.8 CZK bn, 2.6%) and coke and refined oil products (–4.2 bn, 12.4%) in H1.

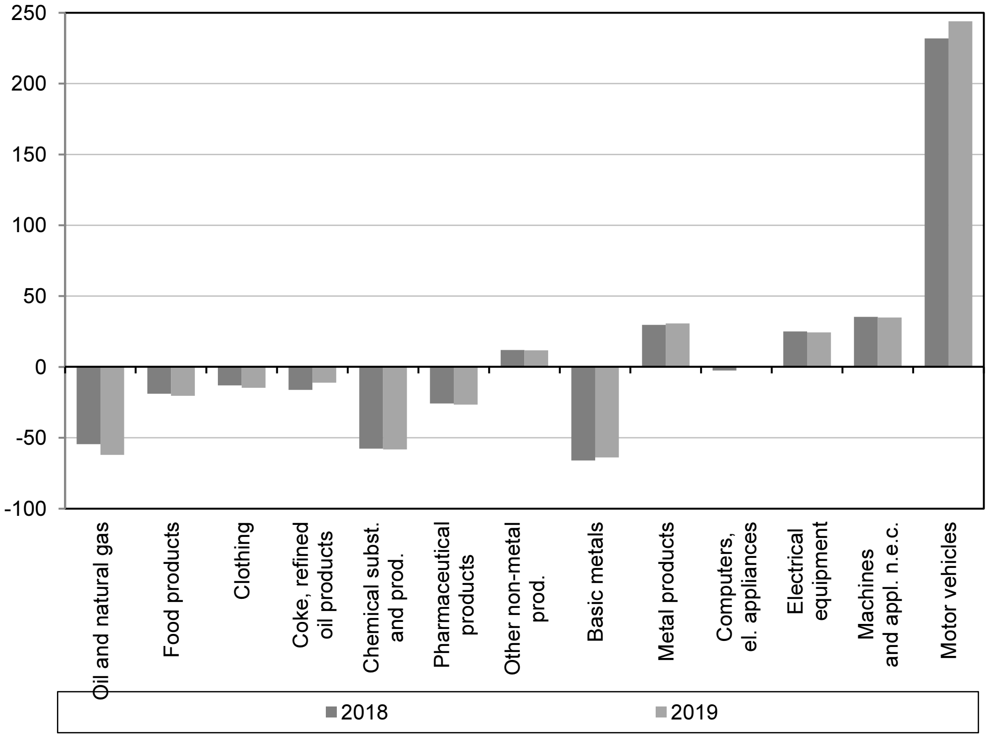
The surplus of the balance of trade with goods expanded in H1, especially due to trade with the EU.

Moderation of the import growth was also apparent in the resulting balance of trade with goods, which summed 108.6 CZK bn in H1 and rose by 17.7 bn year-on-year. Described increase however concerns only Q2. Positive balance increased then by 23.0 CZK bn to 58.4 bn. Series of surplus declines lasting five quarters was thus interrupted. From the territorial perspective the massive increase of surplus with the EU countries by 46.5 CZK bn is mostly of interest. In the opposite direction, the already negative balance with countries outside the Union worsened by 27.1 bn. The surplus of trade with Germany (by 15.4 CZK bn in H1, in that by 13.4 bn in Q2) and with Slovakia (by 18.7 bn in H1, in that by 9.1 bn in Q2) rose thanks to the decreased import described above. Deficit with China (–14.4 CZK bn for the whole half-year) and with Turkey (–7.5 bn) markedly deepened.

Sale of motor vehicles recorded the largest surplus growth.

Sale of motor vehicles (in total +12.1 CZK bn, in that +8.2 bn in Q2), other transport equipment (+8.4 bn, +8.0 bn in Q2), coke and refined oil products (+5.2 bn, +4.8 bn in Q2), basic metals (2.1 bn) and electricity, gas, steam and air conditioning supply (+4.0 bn) mostly contributed to the surplus growth in H1. Trade with oil and natural gas (-7.6 CZK bn) on the contrary mostly more markedly worked in the direction of the deficit.

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



Source: CZSO *in national conception

5. Prices

Growth of total price level accelerated in Q2.

Total year-on-year increase of total price level in the economy (gauged by the GDP deflator) arrived at 3.5% in Q2 2019, the most since Q1 2009. Domestic demand mostly shared in the growth of the price level. Prices of consumption goods grew by 3.8%, in that it was 3.0% for household consumption and goods and services consumed by the government sector featured prices higher by 5.6%. Prices of capital goods rose by 2.6% year-on-year. Terms of trade move close around the level of 100% since the beginning of year 2019. They amounted to 100.3%[39] in Q2.

Consumer prices grew by more than 2% pace in the whole H1.

Year-on-year growth of the consumer price index balanced markedly above the two percent level in H1 2019. Compared to the same period of the last year, the consumer prices climbed by 2.8%. The division housing, water, energies, fuels maintained the largest influence over the price dynamics throughout the whole H1. Prices of food and non-alcoholic beverages and also the division other goods and services contributed to the growth more significantly. Divisions alcoholic beverages and tobacco and accommodation and restaurants also exerted a smaller contribution. Consumer prices rose by 2.8% in Q2 itself. Effect of prices of housing, water, energies and fuels and also food strengthened in Q2.

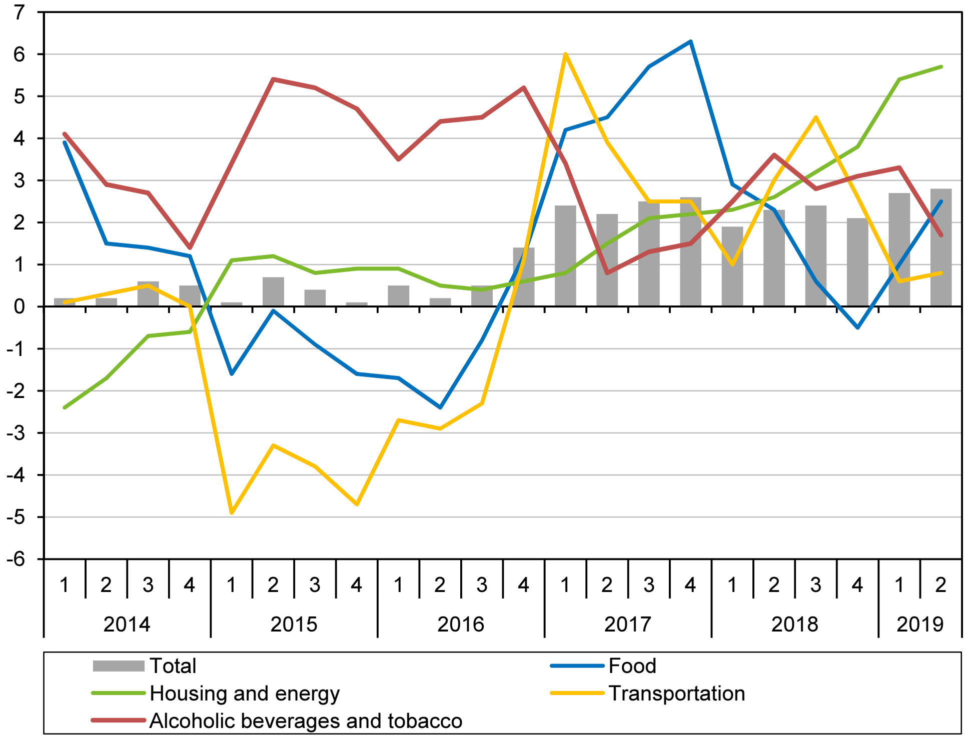
Housing maintained a dominant influence on the total growth.

Prices of housing, water, energies and fuels grew by 5.6% year-on-year in H1. Year-on-year dynamics sharply accelerated since the beginning of the year and peaked in March. In Q2, however, it still maintained a high level. Year-on-year growth of the rents from flats mildly strengthened (3.6%) in H1 compared to last year. The imputed

[39] According to the national accounts data

rent for housing (5.7%) as well as prices of common maintenance and repair of household goods (4.9%) hiked up. Acceleration of prices of the whole division can be ascribed to the dynamics of prices of electricity and heat, gas and other fuels. These have picked up steam since the beginning of the year and grew by 6.9% for the whole half-year. Growth of housing and energies was 5.7% year-on-year in Q2.

Chart 10 Prices in the selected divisions of the consumer price index (y/y in %)



Source: CZSO

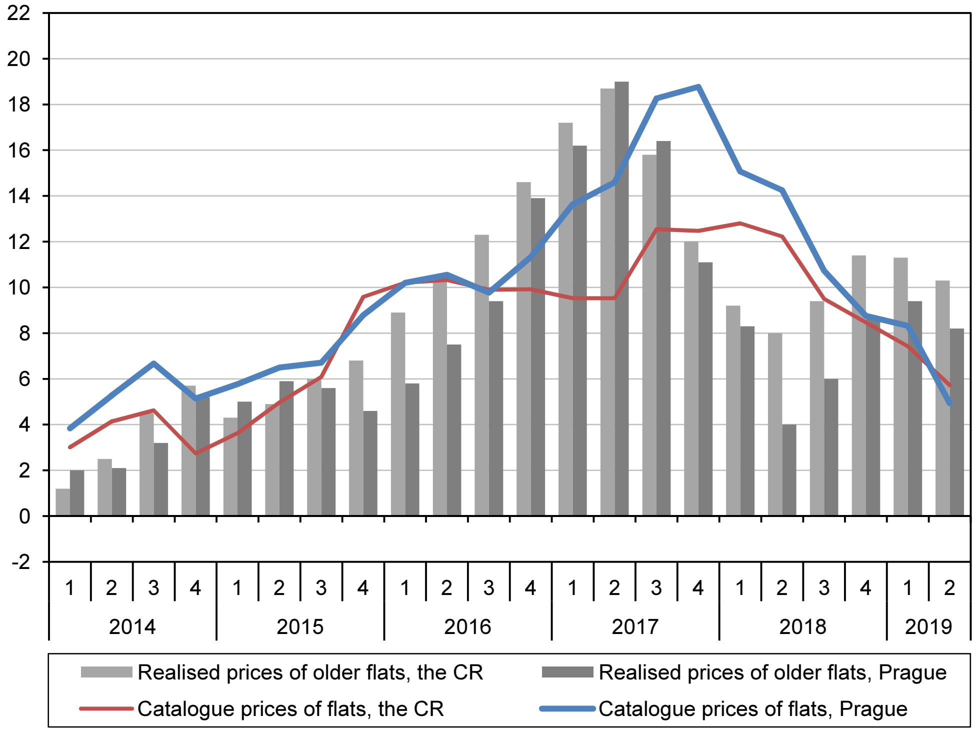
Other items of the consumer basket contributed to the growth less.

Prices of food and non-alcoholic beverages were raised by 1.7% year-on-year in H1. The dynamics between Q1 and Q2 showed a very large difference. Year-on-year growth gained pace in Q2 and reached 2.5% in total. Vegetables, which share only small proportion in the basket, pulled the price growth in this division throughout the whole half-year, but its prices went up by 23.7% in H1. Prices of baking products and cereals also increased (2.7%). In the opposite direction, fruit pushed the prices down (drop by 9.2% in H1) and also sugar, jam, honey, chocolate and sweets (–4.6%). Prices of alcoholic beverages and tobacco rose by 2.5% year-on-year in H1. Growth however slowed to 1.7% during Q2. Prices of household equipment, appliances and their repairs were raised by 1.3%, also mildly contributing to the total growth of consumer prices in H1. Prices of transport stagnated during the whole H1 (0.7%), especially due to the drop of prices of transportation service activities by 7.9%. Prices of wearing apparel and footwear pressed the consumer prices in the downward direction (prices dropped by 1.5%).

Growth of consumer prices mildly increased in the EU in Q2.

Year-on-year growth of the consumer prices reached 1.6% in the EU in H1. In Q2 itself however it slightly speeded up against Q1 to 1.7%. Year-on-year growth dynamics pointed to brisk growth in most EU countries in Q2. It was the most in Poland (from 1.2% to 2.2%), Estonia (from 2.3% to 3.0%) and Hungary (from 3.2% to 3.8%). Growth of prices of food accelerated in case of Poland and Estonia (both countries were struck by African swine fewer), transportation price growth had an effect in Hungary. Romania (4.3%), Hungary (3.8%) and Latvia (3.3%) experienced the highest price growth in Q2. Cyprus, Portugal and Greece (similarly by 0.6%) recorded on the contrary only slow price growth.

Chart 11 Prices of real estate (year-on-year change, in %)



Source: CZSO

Growth of the supply prices of flats weakened.

Development of real estate prices mirrors to a certain extent the situation on the residential market. Supply prices increased by 5.7% year-on-year in Q2 and the trend of the slowing dynamics thus continued (prices grew by 7.4% in Q1). Growth of the supply prices of flats slackened even more in Prague (from 8.3% in Q1 to 4.9%). On the other hand, the year-on-year rate of growth of the realised prices of older flats stays above 8% in the last three years. This index thus increased by 10.3% in total in the CR in Q2 and by 8.2% in Prague. It shows, that even though certain market downturn (connected among other things to worse accessibility of mortgages) was evident in the supply, the position of buyers is still relatively weak. Shortage of suitable flats, which would satiate the demand, still does not enable more meaningful negotiation regarding the price, which could hamper the growth of the realised prices.

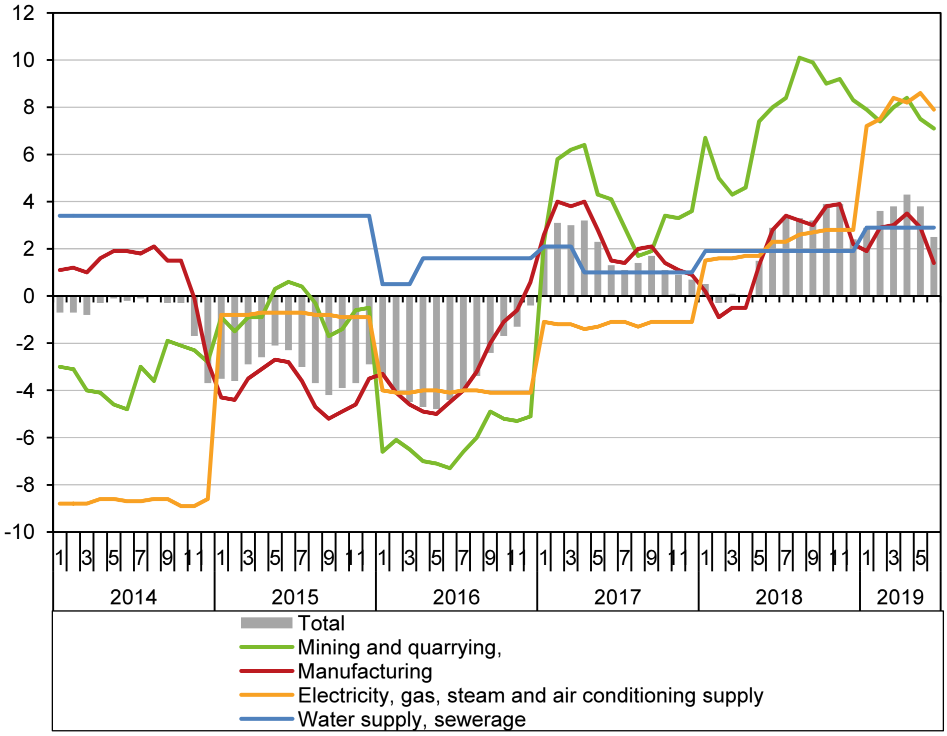
Industrial producer prices were rising in H1.

Prices of industrial producers rose by 3.5% year-on-year in H1. Growth attained the same values also in individual quarters. Goods and services of manufacturing, which holds the strongest weight in the Czech economy, contributed the most to the growth of prices. Their prices rose by 2.6% in H1. Prices of coke and refined oil products, but also food products, beverages, tobacco (year-on-year growth of 3.3%), rubber and plastic products (3.7%) or basic metals and metal products (2.2%) strongly contributed to this growth. Prices of electricity, gas, steam and air conditioning supply, where the strong dynamics from Q1 even strengthened in Q2 rose notably (8.0%). Prices of mining and quarrying were also growing in the first half of year (7.7%). Year-on-year growth of the prices of water supply and water waste management (2.9%) was also higher compared to the last year.

Manufacturers noted a drop in the year-on-year price dynamics in the EU in Q2.

Producer prices in the European twenty-eight increased by 2.5% year-on-year in H1. A significant slump in dynamics however occurred between the Q1 and 2. While the prices rose by 3.1% in the EU year-on-year in the first quarter of the year, the addition fell to 1.9% in Q2. The described slowdown was common to the overwhelming majority of EU countries. A more detailed view then shows a sinking dynamics for mining and quarrying (from 4.3% in Q1 to –0.1% in Q2), the growth of prices in manufacturing also slightly slowed down (from 1.6% to 1.2%) and the addition in energetics decreased from 8.8% to 4.6%[40]. The producer prices were growing the fastest in Romania (5.8%), in Latvia (5.5%) and Hungary (5.0%) in Q2. Producer prices grew only by 0.3% in Portugal in Q2. Only moderate dynamics was also in Austria (0.7%), Greece and Denmark (similarly 0.8%).

Chart 12 Prices of main groups of industrial producers (year-on-year change, in %, based on CZ-CPA classification**)**



Source: CZSO

Prices grew in the majority of market services branches.

Year-on-year growth of prices of market services hiked up to 2.6% already in Q1 and maintained this level in Q2. Prices of land and pipe transport (increase of 3.0% in Q2) comprised the largest contributors to the dynamics. Prices of freight rail transport featured the highest year-on-year growth (to 10.8%). Services in the area of programming and consultancy activities (4.4% growth in Q2) and then insurance, reinsurance and pension funding (6.5%) were further categories, which significantly added to the growth of market services prices. Advertising and market research (growth slowed to 3.9%) and activities of employment placement agencies (7.1%) exerted a moderate influence. Most types of services featured a price growth, only storage and support activities in transportation (–1.6%) worked in the direction of decrease.

Prices of agricultural production picked up steam in Q2, both in the plant and animal production.

Year-on-year growth of the agricultural producer prices markedly accelerated in Q2 and attained 11.0%. This is the most since Q3 2017. Prices of plant (16.6%) as well as animal production (5.4%) were climbing up. The adverse development of harvest in the last year fully manifested in the plant production. Large increase of prices was observed for cereals (16.4%), especially wheat (17.8%) and barley (16.4%). Prices of industrial crops increased by 15.0%, in that prices of oil plants by 15.6%. On the contrary, increase of feed crops shrank to 5.9%. Dynamics of potato prices still accelerates – after 47.9% rise in Q1 to 74.7% in Q2. In that, prices of ware potatoes went up by 104.7% year-on-year in Q2 and seed potatoes by 17.2%. In contrast, the

[40] Section D – manufacture of electricity, gas, steam and air conditioning supply

prices of fruit fell by 21.9%. Prices of animal production climbed back after four quarters of declines, especially due to prices of pigs and piglets. These grew by 13.0%. It resulted from the veterinary situation on the large world markets[41], which caused the supply of pork to be considerably limited. Among the animal products, prices of milk went up by 6.2%.

Prices of foreign trade went up.

Prices of export grew by 2.3% year-on-year in H1 2019, in that by 1.7% in Q2. Especially the price growth of other materials[42] (from 0.8% in Q1 to –1.5% in Q2) and also mineral fuels (from 8.9% to 2.4%) slowed. Price growth of exported machinery and transport equipment (1.4%) and semi-finished products[43] (1.4 %) was also only moderate in Q2. And vice versa, prices of food and live animals (3.5%) and industrial consumption goods (4.3%) went up relatively fast. Import prices followed a similar pattern. They increased by 2.2% year-on-year in H1 and the growth slackened to 1.5% between quarter 1 and 2, mainly due to the effect of prices of mineral fuels (8.0% and 1.0% in individual quarters). Dynamics of prices of other materials however remained very strong (8.7%). Prices of import of food and live animals (3.1%), chemicals and chemical products (1.3%) and machinery and transport equipment (2.4%) also increased year-on-year in Q2. Prices of industrial consumer goods stagnated (0.3%) and prices of beverages and tobacco considerably fell (–5.0%).

Terms of trade were positive in H1.

Terms of trade attained the value 100.2% in both quarters of 2019. Mostly beverages and tobacco (108.1%) and industrial consumption goods (104.0%) worked in the direction of positive terms of trade in Q2. Positive terms of trade of food and live animals (100.4%), mineral fuels (101.4%) and semi-finished products (101.5%) were less pronounced. Trade with other materials (90.6%), chemicals (99.1%) and machinery and transport equipment (99.0%) featured negative terms of trade in Q2.

6. Labour Market

Strain persisted on the Czech labour market. Shortage of spare capacities steered businesses more and more towards importing labour force from abroad.

Perceptible strain reflecting the imbalance between the supply and demand prevailed on the Czech labour market also during H1 2019. Demand for employees still remained strong despite partial corrections. Their shortage still presented the main growth barrier across the majority of branches, it was the most acute in construction. Supply of new workers has been considerably limited on the domestic market for already several quarters. Businesses thus gradually redirected their recruitment activities towards foreign workers, assisted by the activities of the state, continued in the targeted projects of economic migration[44]. The role of foreigners on the Czech labour market thus further grew[45]. However, businesses still faced considerable obstacles to acquire new more qualified workers. Both new and current employees benefited from this situation – their earnings showed a significant growth

[41] African swine fever, which afflicted China, but also some European countries. According to the State Veterinary Administration, occurrence is currently reported (July 2019) from 9 EU member states: Belgium, Bulgaria, Estonia, Italy (presence only on Sardinia), Lithuania, Latvia, Hungary, Poland and Romania.
[42] Inedible raw materials, except for fuels.
[43] Assorted market goods mainly based on material.
[44] Increase of quota for qualified workers from Ukraine occurred for instance during the year 2018 (from 9.6 thousand to 19.6 thousand). The scope of countries, whose citizens can enter the schemas as well as projects targeted at qualified workers, also widened (for India, the Philippines, Mongolia and Serbia). Further increase of quota for workers from Ukraine came into force during the summer time of 2019 (to 40 thousand).
[45] 659 thousand of citizens with foreign citizenship were employed according to the data of MLSA and MIT (Ministry of Industry and Trade) in the CR at the end of year 2018. They already comprised one eight of all workers on the labour market. Their number was further increased during the first half of year 2019, as indirectly evidenced by demographic statistics – the positive balance of total foreign migration (20.9 thousand persons in H1) as well as the increase of the number of all registered foreigners (by 8.4 thousand according to the Foreign Police Directorate since the beginning of year 2019). Similarly to the whole last year, Ukrainians contributed the most to the higher number of all working foreigners.

Number of employed in the economy hiked up to the record level at the beginning of the year, where it already remained in Q2.

Total employment[46] in the economy further boosted this year, rate of growth however lowered. While the number of employed increased by 1.4% year-on-year in Q1 (similarly to the whole last year), it was already only 0.8% in the subsequent quarter (the least since Q3 2014). Number of workers again set a new record in the era of independent CR in Q1 2019 (5.48 mil.), this level however remained stable in the next time period. Slowdown was aligned with the results of the business cycle surveys, which signalled more prudent attitude of businesses to hiring new workers already during year 2018 (mainly in industry, but also in some branches of market services)[47].

Business cycle survey implied continuing positive expectations of employment especially in construction and trade.

This tendency reflected both the growing uncertainties of significant domestic exporters linked to the current situation in the euro area as well as longstanding pressure on raising the labour productivity driven by growing wage costs as well as falling profitability of businesses. More cautions outlooks of businesses in terms of employment were apparent also at the beginning of this year, Q2 witnessed a stabilisation. Nevertheless, the short-term anticipations of employment remained patently positive especially in construction and trade[48].

Employees caused exclusively the higher number of workers.

Year-on-year expansion of total employment (+60.6 thousand) was the result exclusively of higher number of persons with the employee status in H1, since the number of self-employed stagnated (among main branches it more substantially increased only in information and communication activities, finance and insurance activities, professional, scientific, technical and administrative activities and also in manufacturing). Core of the total employment growth was further shifting into the tertiary sector, which profited from the growing domestic demand as well as expanding tourist industry. Services sector contributed to the higher number of workers in the economy nearly from three quarters.

Dynamical growth of branch information and communication lasted, branches with the predominant public sector also created new job positions.

Dynamic development of information and communication continued (+4.2% year-on-year). The activity was bolstered by nearly 24 thousand of job positions and total employment expanded by one sixth in the last five years. Branches with the predominant public sector also fared well (+2.3%), mostly due to education as well as health and social care. Weight significant group trade, transportation, accommodation and food service (+1.2%) showed a weaker dynamics in comparison to the last year, partly due to the mild lowering of number of entrepreneurs (without employees).

Rate of growth of employment weakened in industry, in contrast further accelerated in construction.

Manufacturing enlarged by 0.8% of workers, this branch records below average pace already for two and a half years[49]. Construction was hiring workers already second year in a row and even though the employment growth (+1.0%) remained slightly below the pace of the whole economy in this branch also this year, it represented the best half-yearly result here since the end of year 2010. Trend of a very gradual reduction of the number of workers in the primary sector continued, largely due to the reduction of number of self-employed (similarly to the last year).

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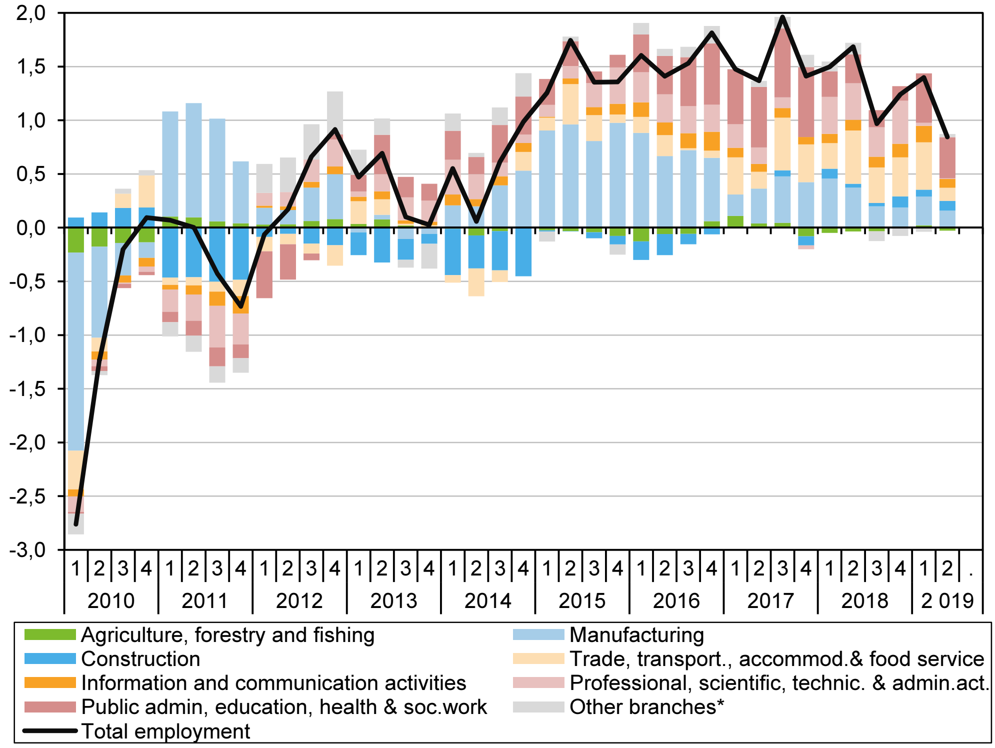
[46] Unless stated otherwise, data regarding employment are stated in the national accounts conception adjusted for seasonal effects in this chapter.

[47] Expressed according to the seasonally adjusted data from the business cycle surveys as the difference (in p.p.) between the proportion of businesses expecting employment growth in the next three months and businesses on the other hand anticipating decline of their levels of employees.

[48] Balance of short-term expectations in the area of employment reached +15 points in both construction and trade in June 2019. It was similarly –2 points in industry and market services. Situation differed according to sub-branches. Within manufacturing, the largest share of businesses expecting reduction of their number of workers was in manufacture of fabricated metal products, machinery and manufacture of wearing apparel. On the other hand, positive outlook prevailed mainly in manufacture of computers, electronic and optical products, in chemical, pharmaceutical and wood industry. Among market services, mainly businesses in information and communication, in professional, scientific and technical activities and further also in sub-branches storage or restaurants signalled growth. On the contrary, businesses in transportation, postal and courier activities, financial activities (except for insurance and pension funding), travel agencies and also security and investigative activities were more inclined to the reduction of number of workers.

[49] According to the business statistical data, the number of employees even mildly fell (by 0.3%) in industry in H1. In this conception however agency workers are not included in the industry and the effect of the shadow economy is also not allowed for.

Chart 13 Total employment (year-on-year in %) **and contributions of main branches to year-on-year employment change** (in percentage points)



*Includes branches: Mining and energetics; Financial and insurance activities; Real estate activities; Arts, entertainment and recreation activities; Other services.
Source: CZSO (national account

Average age of workers was further rising. Employment rate of population in the productive age also grew, but slower.

From the view of the age composition, the employment was favourable impacted mainly by the growth of both the legal and real age of retirement. Further structural changes also continued – strong population cohorts of the 70s were moving into the age with the higher rate of economic participation. Average age of workers further increased. These trends were also reflected in the growing employment rate of productive age population (15–64 years). It arrived at 82.0% for males and 67.8% for females in Q2, it rose by 0.3 p.p. year-on-year in both cases. The rate of growth gradually evaporates as the potential resources of workers among both the unemployed and economically inactive who wish to work[50] „dry out". Still the employment rate stays significantly above average in the CR within the European context. For females, the CR ranks eleventh[51] among the EU states (with maximum in Sweden – 75% and minimum in Greece – 46% and further Italy – 50%), for males second (tightly behind the Netherlands).

Employment rate of both males and females in the CR ranks among the significantly above average in the EU in the long-term.

General unemployment rate kept further mildly falling, mainly due to females. Proportion of long-term unemployed among all unemployed persons stabilised closely above 30%.

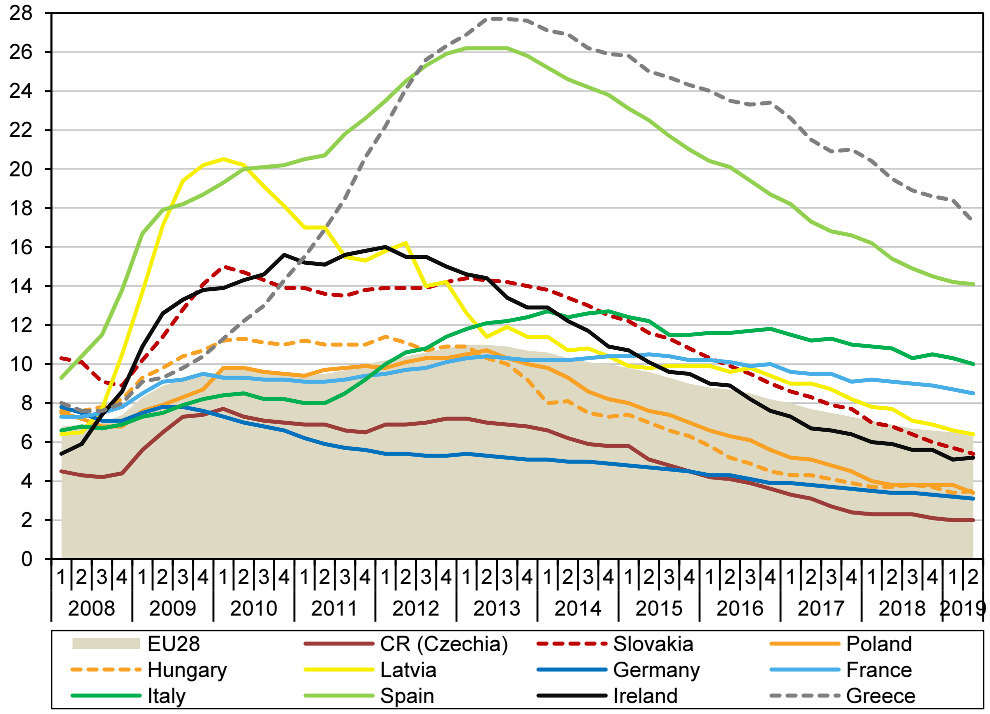
General unemployment rate (after seasonal adjustment) was already falling only slowly this year, similarly to year 2018. It reduced to 1.7% for males, 2.5% for females in Q2 2019. Year-on-year it thus fell only by 0.1, resp. 0.4 p.p. Positively, the number of long-term unemployed (above one year) also decreased, however already only by 2.7 thousand of persons in Q2 itself. These persons thus added only one sixth to the year-on-year reduction of total unemployment. They were represented among unemployed then only by one third and this share has not changed for nearly two years. Persons aged above 50 and also persons with primary education hold higher proportion among long-term unemployed. Even though the number of businesses expecting reduction of the level of employees mildly increased during this year, it can be assumed, that the labour

[50] Persons not in employment, not seeking work (thus not fulfilling a condition to be put among unemployed), but expressing the willingness to work (regardless of the ability to join new employment fast). There were 105 thousand of them in Q2 2019, nearly by one half less compared to years 2010 and 2011, when the labour market was hit by the aftermath of the economic recession.
[51] Only women in Baltic countries attained a higher employment rate (70 to 72%) among states that accessed the EU after year 2000, mainly due to the higher legal retirement age.

Unemployment rate of both males and females in the CR still stayed the lowest among the EU states. Other countries of central Europe also enjoyed a very good position.

market managed to again absorb these so far sparse groups of dismissed employees without difficulties. Very low unemployment is also manifested in the improved working conditions of current employees (e.g. drop of share of employees working involuntarily on temporary contract, specifically for agency workers as well). Unemployment rate of both males and females in the CR boasted the lowest values among the EU countries this as well as last year. Unemployment was falling to the minimum (since the beginning of 90s) the same as in the CR also for instance in other countries of the "Visegrad Group".

Chart 14 General unemployment rate for persons aged 15 to 74 years in the CR, total EU and selected Union countries (in %)*



*Data after seasonal adjustment. Source: Eurostat

Number of job vacancies in the supply of labour offices neared 350 thousand, their rate of growth however slackened substantially since the half of 2018.

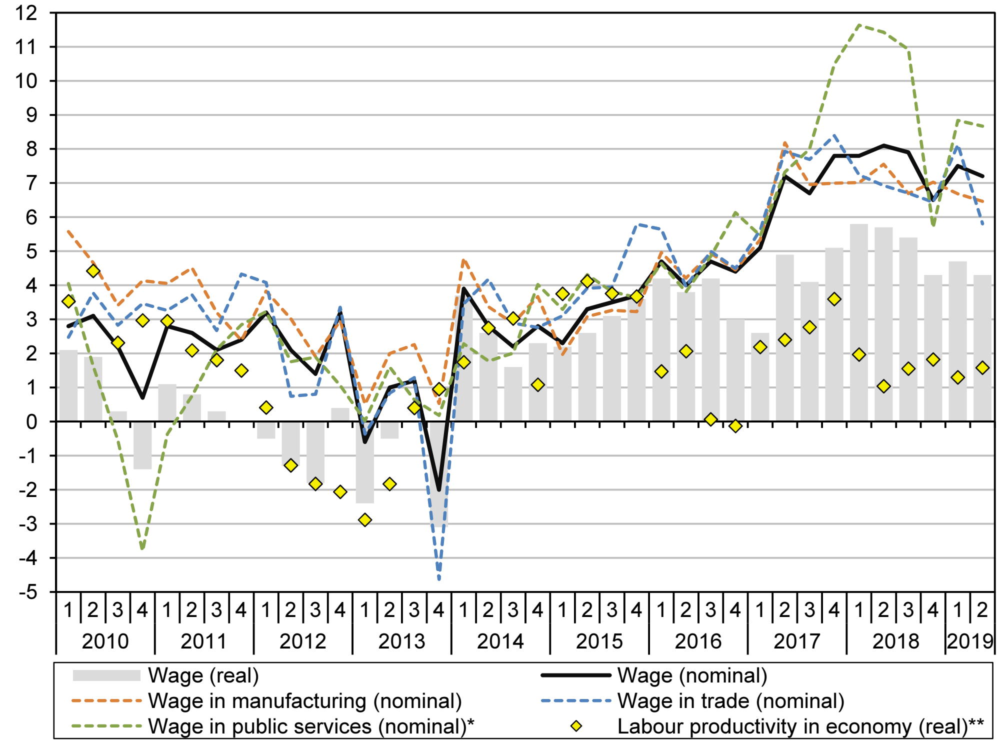
High demand for employees is evident from the rising number of job vacancies offered by the labour offices. There were 342.5 thousand of job vacancies at the end of June 2019, by 41 thousand more year-on-year. Speed of growth of number of positions however considerably slackened for the last year, their number even slightly lowered month-on-month in June (for the first time since the end of 2016). Dramatic imbalance of the job additions from the view of the qualification demands as well as regions attained already in the previous years further deepened, when the supply of new positions likely for the most part aimed at foreign workers from economically less developed countries. Already 77% of all job vacancies belonged to classes with the low qualification (craftsmen and repairmen, machine operators, supporting and non-qualified staff). Similarly 69% of all jobs targeted applicants with maximally the primary or lower secondary education, 20% then apprentices. On the other hand only minimum shift was observed in the supply for persons with higher education, but also e.g. for persons with disabilities.

New job vacancies targeted primarily persons with lowest qualification.

Excess of demand over supply of labour force, which has been apparent at the level of the CR already since April 2018.

Ratio of job applicants to one job vacancy was 0.6. Excess of demand over supply of labour force, which has been apparent at the level of the CR already since last year´s April, was signalled by two thirds of districts and majority of regions (apart from Ustecky and Moravian Silesian) in June this year. Excess pressure of applicants nevertheless still prevails for persons with the school leaving certificate (1.9) and university education (1.3) and for specific groups of applicants – women on parental leave or persons with disabilities (2.7).

Chart 15 Average nominal and real wage and labour productivity** (year-on-year in %)



* Includes branches: Public administration, defence, social security; Education; Human health and social work activities; Arts, entertainment and recreation activities.
**Calculated as the share of seasonally non-adjusted GDP and total employment (in the national accounts conception).
Source: CZSO (national accounts)

Factors promoting brisk growth of wage were still more prominent in the domestic economy.

In spite of more urgent „import" of foreign workers, domestic employers still faced considerable difficulties in their staffing process. Higher fluctuation was also likely in play mostly with less qualified workers, which results from the fact, that these positions were taken by persons less established on the domestic labour market (foreigners, long-term unemployed). These factors together with the repeated increases of the minimal wage were contributing to the high wage dynamics. However, chances for its sustaining kept further narrowing due to falling profitability of businesses enhanced by the worsened economic development in key export destinations.

Rate of growth of average nominal wages slightly slowed this year compared to H1 2018, due to the effect of manufacturing and public services.

Wages notably gained pace in financial activities.

The average gross nominal monthly employee wage went up by 7.2% (based on business statistics) year-on-year and climbed slightly above 34 thousand CZK in Q2 2019. Growth reached 7.3% for the whole half-year (it was 8.0% in the same period of year 2018). The highest wage growth among main branches displayed arts, entertainment and recreational activities (12.0%). However, growth within this branch was concentrated in the segment outside the area of public services. There earnings grew the most in education (nearly by 10.6%), still their average monthly size somewhat lagged behind the level of the national economy. Wages grew briskly also in administrative and support service activities (+8.7%), their level was, however, by one third lower compared to the whole economy. Wage pace in financial and insurance activities (+8.1%) markedly improved after four years of below average growth. It was the consequence not only of the extraordinary bonuses tied to the very good business results of year 2018, but also the strong pressure on the labour productivity, which resulted in reduction of the registered number of employees (by 1.9%). It was also valid for manufacturing (–0.4%), volume of paid out wages was here the third lowest (+6.2%) among nineteen main branches (after branches of the primary sector). Average wages in the developing branches with so far below the level of whole economy – trade (+6.9%) as well as construction (+6.8%) also grew by a relatively weaker rate of growth.

Growth of purchasing power of wages mildly slowed year-on-year, still it remained high.

Wage median increased by 7.2% year-on-year in H1 and it lagged behind the pace of the average wage for the first time since H1 2015. Even though the slightly picking inflation „cut“ whole two fifths from the earnings growth this year, real value of average wages was by 4.4% higher year-on-year. Within first half-years, it presented the third strongest pace for the last sixteen years (after years 2007 and 2018).

7. Monetary Conditions

Monetary policy-relevant rates were again raised in Q2.

While the setup of basic monetary policy-relevant rates did not change in Q1 2019, it was decided to increase the two-week repo rate from 1.75% to 2.00% in May. Discount rate (to 1.00%) and Lombard rate (3.00%) also increased. The difference between the rates in the CR and in the euro area thus further widened (ECB did not change rates since March 2016 and repo rate is zero). The koruna foreign exchange against euro was in contrast to dollar or pound relatively stable throughout the whole half-year (it moved in the corridor between 25.40 and 25.90 koruna per euro[52]). The rate was then mildly weakening from April to May 2019 (maximum value of 25.86 CZK/EUR on the 29th May). Subsequently, the trend turned and the koruna foreign exchange appreciated up to the level of 25.44 CZK/EUR until 27th June. The koruna foreign exchange against dollar was weakening from January to May down to 23.15 CZK/USD on 31st May. Koruna however appreciated during June and completed the half-year at the level of 22.36 CZK per dollar.

Interests on government bonds fell.

Interbank interest rates also naturally reacted to the growth of the monetary policy-relevant rates. Three-months PRIBOR rate increased by 0.14 p.p. to 2.17% during Q2. In the opposite direction, the yields of bonds were decreasing, specifically for all types of maturities. Short term government bonds (2 years) bore interest 1.52% as of 30.6., by 0.19 p.p. less compared to the end of March. Medium term bonds (5 years) featured more significant fall – by 0.27 p.p. to 1.43%. Yield on long-term bonds decreased by 0.24 p.p. to 1.58%. Euro area bonds were also characterised by falling trend – the short term ones aimed deeper below the zero level (–0.34% as of 30.6.).

Interest rates on deposits with agreed maturity continued to grow.

Development of interest rates on client accounts did not divert from trends set in the last year. Interest rates on the current accounts of households remained practically unchanged (0.05% to 30.6.). On the contrary, the interests on deposits with agreed maturity mildly rose (by 0.08 p.p. to 1.54% as of 30.6.) also in Q2. Exclusively the rates on accounts with agreed maturity up to 1 year (inclusive) grew, other maturities recorded a decrease in Q2. Interest rates on current accounts of non-financial businesses followed a different path. They were rising five quarters in a row and attained on average 0.22% as of 30.6. For non-financial businesses, interest rates also increased on deposits with agreed maturity (by 0.28 p.p. to 1.63% during Q2) as well as deposits redeemable at notice (by 0.1 p.p. to 1.35%).

Volume of deposits expanded markedly in Q2 year-on-year, especially due to the deposits of government institutions.

Total volume of deposits expanded by 514.4 CZK bn year-on-year in Q2. It is the most since Q3 2017. Deposits from residents expanded, on the contrary non-residents were withdrawing their deposits – their volume shrank by 8.2 CZK bn year-on-year in Q2 (total deposits of non-residents fell by 40.6 bn year-on-year during H1). Deposits of all sectors enlarged, government institutions however contributed the most to the year-on-year acceleration of dynamics. These doubled their deposits to 630.8 CZK bn between the end of year 2018 and 30th June 2019. According to the time perspective, the year-on-year growth of the volume of term deposits accelerated in Q2, even though part from the 35.4% increase can also be ascribed to the

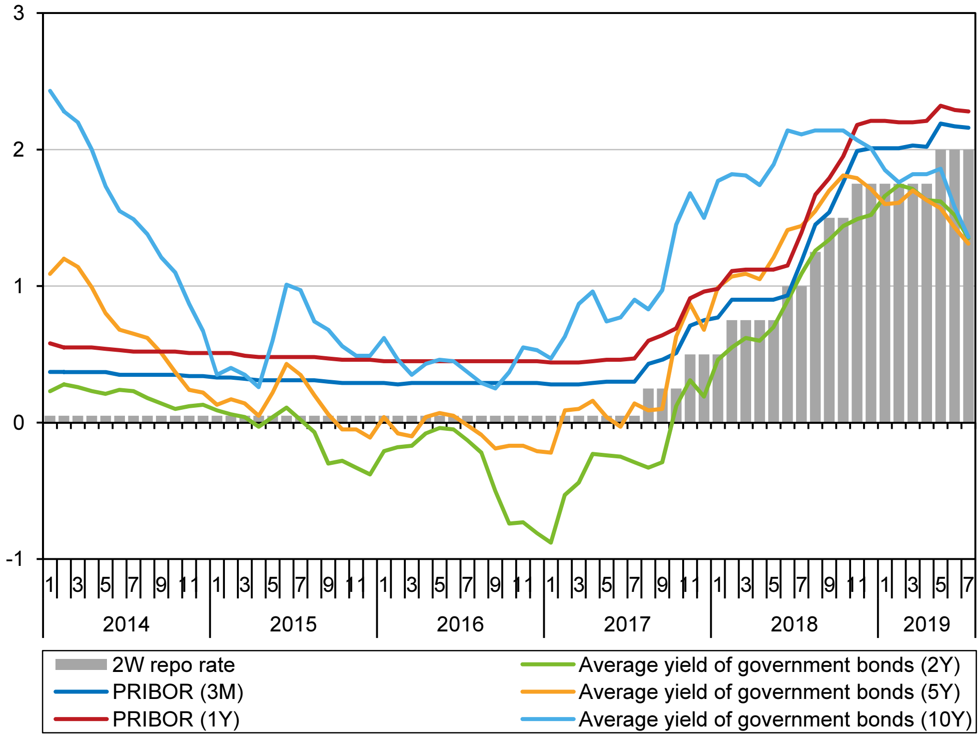
[52] Unless stated otherwise, public database ARAD of the Czech National Bank is the source of data in this chapter.

methodological changes[53]. The growth focal point lay mainly in the short-term deposits, which also corresponds to the development of the interest rates.

Interests on credit to households again fell.

Following a short period of growth in Q2 to Q4 last year, the average interest on credit to households was cut in H1. Interests fell by 0.23 p.p. to 8.4% quarter-on-quarter in Q1 and further down to 8.37% until 30.6. Conditions of mortgages for households also became slightly more advantageous in Q2, the average interest fell by 0.1 p.p. to 2.87%. Especially prices of loans fixed for a medium term were cut – above 1 year up to and including 5 years by 0.08 p.p. and above 5 years up to and including 10 years by 0.13 p.p. It was possible to observe similar development for interests rates on credit to non-financial businesses. They grew in the last year and attained their maximum on 31st March 2019. The average interest on credit to non-financial businesses however again fell in Q2, mainly under the influence of large loans (above 30 CZK mil). Their average interest rate fell by 0.12 p.p. to 3.11% during Q2. Subtle decrease was also recorded in case of credit up to 7.5 CZK mil. The interest in contrast grew for other categories.

Chart 16 Market interest rates (in %)



Source: CNB

Growth of volume of provided consumer credit slackened.

Year-on-year growth of the total volume of credit provided to households remained at bay with 6.7% in Q2 (the pace fell below 7% for the first time since Q3 2016). Growth of volume of provided consumer credit (to 7.7%) as well as credit for housing (7.5%, below 8% for the first time since Q1 2016) slowed. Development of mortgages is distorted due to the re-classification of part of the consumer credit for housing to mortgages[54]. Year-on-year growth of the volume of mortgages thus based on the CNB statistics reached 10.3% in Q2, if we however deduct approximately 20 bn,

[53] According to the CNB commentary, a decrease of credit balances on the current accounts occurred in the bank statistics in January 2019 compared to December 2018, mainly in the household sector. This fluctuation was caused by the one-off re-classification on the part of the reporting entities into savings deposits redeemable on notice.
[54] As a result of modification of the mortgage definition in the amendment to the Act No. 190/2004 Col., on Bonds, effective as of 4th January 2019.

which were transferred between individual types of credit on 1st January, we get an approximate value of 8.5%, less than in the past year. 40.7 thousand mortgage contracts were closed in Q2, by 10.7 thousand less year-on-year.

Rate of growth of volume of credit to non-financial businesses markedly fell.

Volume of credit provided to non-financial businesses (both in CZK and foreign currency) increased in total by 3.5% year-on-year in Q2. Volume of credit in foreign currency again followed a more dynamic development, growing by 6.6%. However, the observed growth markedly narrowed compared to the preceding quarter (all credit grew by 6.2% in Q1, by 14.5% in foreign currency). Volume of credit denominated in CZK rose by 2.2%. Slower growth of the provided credit did not avoid manufacturing (from 6.4% in Q1 to 1.7% in Q2), construction (from 13.7% to 7.6%) or wholesale and retail, motor vehicle repairs and maintenance (from 4.6% to 1.4%). Information and communication kept a strong pace (13.7%).

8. State Budget

State budget ended in deficit in H1, which deepened year-on-year. Brisk growth of current as well as capital expenditures stood in the background, together with mild slowdown of economic growth.

State budget (SB)[55] ended in deficit of 20,7 bn in H1 2019. Budget balance worsened year-on-year for the third time in a row and thus moved into deficit similarly to the last year. While total SB revenues strengthened by 8.1% year-on-year and expenditures by 10.2%, their rates of growth perceptibly exceeded the annual budget anticipations. SB balance, which presents a dominant item of the budget deficit or surplus of the government institutions sector, attained –0.8% in relation to the nominal GDP in H1 (–0.2% a year ago). Deeper deficit reflected this year´s brisk growth of weight significant current expenditures, as well as the acceleration of the investment activity. Moderate slowdown of the economic performance also played a role, since the dynamics of total tax incomes (including insurance) eased its pace to the four-year minimum (+5.9%, +6.2% a year ago).

Insurance receipts as well as higher tax collection positively affected the growth of total revenues, moderate decrease of revenues from the EU budget then negatively.

Year-on-year growth of total SB revenues (by 55.8 CZK bn) was by nearly three quarters pulled by higher tax incomes (including insurance). Non-tax and capital revenues also had a favourable impact (by one sixth higher year-on-year), since the moderate decrease of revenues from the EU budget (by one tenth, resp. 6.6 CZK bn)[56] was offset by a onetime transfer of 18.0 CZK bn from the privatization account. Mainly higher collection of insurance on social security (+20.8 CZK bn) contributed to the stronger all tax incomes (similarly to year 2018), total tax collection enjoyed only slightly weaker effect.

Collection of VAT strengthened during the half-year, but lagged behind both the budget anticipations and final consumption dynamics of government as well as households.

SB raised on the weight dominant tax – VAT – by 3.0% more year-on-year in H1, and even though the growth rate strengthened during the year[57], it still lagged behind the budget anticipations. Pace of VAT collection was slowing already third year in a row and did not approach the growth dynamics of final consumption expenditure of households (5.7%) or government institutions (8.5%)[58] so far. Collection of all consumption taxes rose by 3.9% due to higher collection of all main types of tax. For the most significant tax by volume on mineral oils, it strengthened by 2.3%[59] and managed to stay on the level of budget anticipations thanks to higher dynamics in Q2 itself. Collection of tax on tobacco products

[55] Unless stated otherwise, all data related to the state budget stem from the data of the Ministry of Finance regarding the cash fulfilment.

[56] These revenues also contain the revenues from so called Financial mechanisms *(EEA and Norway Funds, Swiss – Czech Cooperation Programme).* Their decrease in H1 2019 was affected by exceptionally high last year basis – SB acquired part of final payments related to the already concluded programme period 2007 to 2013 (in the amount of 20.4 CZK bn) in H1 2018.

[57] Volume of VAT collection stagnated year-on-year in Q1 2019, it grew by 5.9% in Q2. Slower pace was partially also connected to the year-on-year lower volume of retained excessive deductions by Financial Administration at the beginning of the year. The most up-to-date data so far also proved the dynamism of the VAT collection during this year – VAT collection strengthened in total for the first eight months of the year by 5.2% year-on-year.

[58] Both values express the year-on-year rate of growth of the nominal not-seasonally adjusted consumption for H1 2019.

[59] It also corresponds to the more detailed CZSO data related to the natural consumption of oil products. Consumption of diesel fuel (+2.4%) as well as kerosene (+3.6%) increased year-on-year, decrease occurred on the contrary for petrol (–0.2%) during the first five months of year 2019.

recorded higher rate of growth despite the fact, that the rates were not raised this year (for the first time since 2011). Its collection however fluctuates during the year, mainly for the reasons of frequent prestocking.

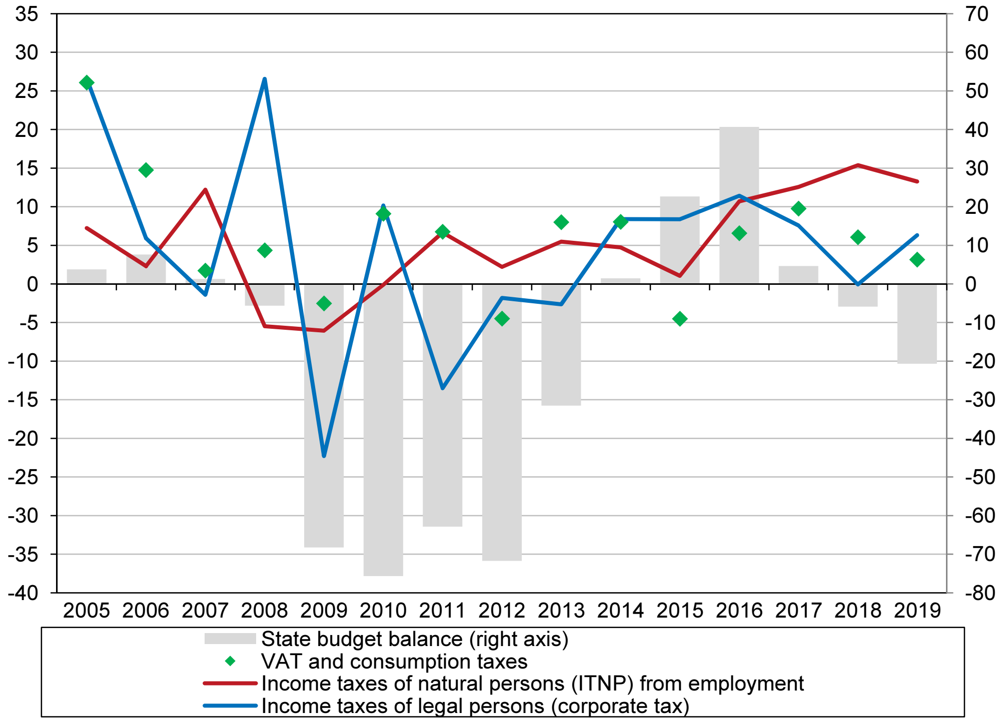
Growth of income tax of natural persons from dependent activity stopped accelerating, its pace still overtook the level of business cycle peak in the last decade.

Income tax of natural persons from dependent activity (employment) further added the most to the growth of the state-wide collection of direct taxes. It strengthened by 13.3% year-on-year, slightly below the level of budget anticipations. Despite the pace of collection not strengthening any more in contrast to years 2016 till 2018, it still exceeded the dynamics from the business cycle peak period in the last decade. Record number of working persons and further also the brisk growth of average earnings, especially in services was also instrumental in this. Tax on capital income also recorded a double-digit growth exceeding the budget anticipation. Collection of income tax of natural persons associated mainly with the volume of sales flowing from small businesses enlarged as well. The swift growth of the domestic demand was still evident here, widening of tax rebates and tax benefits (e.g. on children) had the opposite effect. State-wide collection of the corporate tax rose by 6.3% and reflected the decreasing profitability of businesses, mainly because of intensifying wage costs, but also relatively weaker last year´s basis of this tax.

Positive net position of the CR towards the EU budget hiked to the three year maximum in H1.

Even though a moderate decrease of SB revenues from the EU budget occurred this year compared to H1 2018 (including financial mechanisms), this drop was not related to the current programme period (2014–2020). It is also proved by the net position of the CR towards the EU budget. It attained +24,4 CZK bn in H1 and it was the highest for the last three years in this time period. Considerable increase of revenues (from 32.9 to 53.9 CZK bn) was exclusively behind the strengthening of the net position this year. Size of payments of the CR into the EU budget expanded year-on-year (by nearly one third to 29.6 bn.)[60]. Stronger revenues mirrored faster drawing especially from structural and cohesion funds (+17.5 CZK bn) and also in the programmes aimed at rural development.

Chart 17 State wide collection of selected tax incomes (year-on-year in %) **and state budget balance** (in CZK bn) **in H1**



Source: MF CR

[60] For the most part a varying timing of mandatory payments of the CR within this year stood behind this development, which was connected to the prepared exit of the Great Britain from the EU.

Faster drawing of funds from the EU budget stood behind the strengthened investment activity of the state.

Total SB expenditures increased by one tenth year-on-year in H1, similarly to the same period of year 2018. Both current (+58.1 CZK bn) and capital expenditures (+12.5 bn) added to the growth this year. More than 70% of investment was aimed at the common CR and EU projects[61], their volume expanded by nearly 10 CZK bn year-on-year. Investment drawing has been only 36% of the annual planned budgeted amount at the end of June this year (similarly to last year), mainly because of slower onset of solely national investment (17%). Proportion of investment on all SB expenditures was rising already second year in a row and amounted to 6.0% (average for the whole decade was 6.6%).

Growth of current SB expenditures accelerated mostly due to the effect of higher expenditures on pensions and wages of employees in the budget sphere.

Rate of growth of current SB expenditures strengthened within H1 already third year in a row. It climbed to 8.8% this year, the most in the last thirteen years. Higher expenditures on social benefits shared in it by nearly one third (growth of 22 CZK bn). Expenditures on wages in the regional education (+13.7 bn) also added significantly as well as the wages in the central government institutions including the armed and police forces (+4.4 bn) and further then the non-investment transfers to state funds as well as higher compulsory payments into the EU budget.

Pension account balance slightly decreased, but remained in surplus.

Proportion of social benefits in all SB expenditures totalled 39.2% and it was falling for the second year in a row. Increase of the volume of social benefits was from 86% pulled by the resources on pensions. Their growth rate doubled compared to the beginning of the last year (to 8.8%) and reached a ten-year maximum at the same time. Given the stagnation of the number of persons receiving pensions, the effect of the legislative amendments fully showed[62]. Expenditures on pensions overtook the rate of growth of the collected insurance (+7,8%)[63] for the first time since year 2013. Pension account balance[64] thus mildly worsened, still it remained positive already second year in a row (+7.7 CZK bn).

Growth of expenditures on non-pension social benefits was driven by higher drawing of sickness benefits.

Improvement of the financial situation of households was reflected in the lower SB expenditure on both material deprivation assistance benefits and state social support benefits.

Expenditures on other social benefits (excluding pensions) amounted to 64.9 CZK bn in H1, they increased by 4.8% year-on-year. Their growth rate was expanding already fourth year in a row. This development was considerably affected by the sickness insurance benefits, whose drawing deepened by 15.3%[65] and nearly doubled in the last seven years. They thus became the most significant group of social benefits by weight for the first time after year 2008 when they replaced the state social support benefits (SSS) in this role. Their drawing on the contrary decreased by 2.5% this year, the most in the last seven years. Among SSS sub-benefits, only foster care benefits strengthened. All income-tested benefits (e.g. child allowances) and weight dominant parental allowances (–0.8%) went down. Reduction of expenditures on material deprivation assistance benefits (by 21% year-on-year, by 60% in five years) also emphasised more favourable financial situation of households. The shrinking of expenditures on unemployment benefits on the contrary halted after five years, besides other things also due to high proportion of its friction component and growth of the size of average monthly benefit (derived from previous job earnings of the job applicant)[66].

[61] Total expenditures (incl. current) to finance common EU and CR programmes summed 65.8 CZK bn in H1, by 15.2 CZK bn more year-on-year.

[62] It included the increase of the basic pension assessment from 9% to 10% of the average wage, percentage pension assessment by 3.4% and further the increase of 1 000 CZK for pension recipients, who reached the age of 85 years. Pension adjustment mechanism further fully reflects the impact of the consumer price growth (altern. the growth of the living costs of pensioners) since year 2018 and one half of the growth of real wages in the economy is also taken into account.

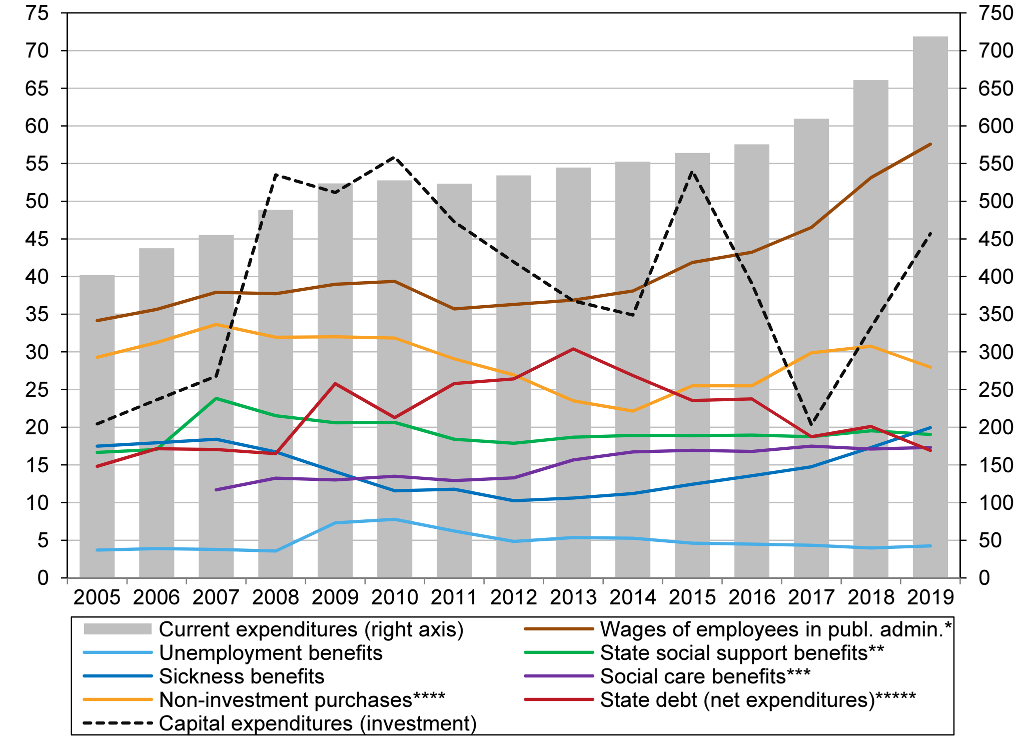
[63] Rate of year-on-year growth of levied insurance on pensions slowed this year for the first time after five preceding years. It jumped to record +10.7% in H1 2018. This development corresponded to the moderate slowdown of employment growth in the economy as well as likely peak of average wage dynamics achieved last year.

[64] Expressed as the difference between revenues and expenditures on pensions from the SB. Expenditures on administration of the pension insurance system are not included (they arrived at 6.4 CZK bn according to the MF data for the whole year 2018).

[65] Continuing growth of the temporary incapacity for work stood behind it (based on the MLSA data, the number of reimbursed days of sickness leaves increased by 6.7% in H1). Daily assessment basis of this benefit also increased (derived among other things from the size of previous earnings). Growth of the volume of paid out sickness benefits was also affected by higher drawing of maternity benefits (+7.5%).

[66] 34.7% of all registered job applicants were eligible for the unemployment benefits at the end of June 2019, 29.7% the year before. The average monthly size of the benefit amounted to 8 011 CZK in June 019, 7 382 CZK in the same time period of the last year.

Chart 18 Selected half-year state budget expenditures (in CZK bn)



*Cover expenditures on salaries in central government institutions (including armed and police forces). Do 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, MLSA

Size of the state debt remained stable. Borrowing need was realised via issue of medium and long-term bonds on the domestic market.

Trend of decrease of net expenditures on state debt continued.

State debt reached the size of 1 712.6 CZK bn at the end of June 2019. Year-on-year it nearly did not change, it mildly fell compared to the preceding quarter (by 1.1%). State kept realising its borrowing need exclusively on the domestic market. CZK value of the foreign debt thus narrowed year-o-year (by 38.6 bn) and the share of external debt in total indebtedness arrived at 12.6%, which was the least since the end of 2004. State issued medium- and long-term bonds in the amount of 200.6 CZK bn during H1, more than three fifths of them had maturity above 10 years. State used the opportunity of favourable conditions on the domestic financial market (yield of state bonds along the longer end of the yield curve hit the lowest level since the end of year 2017). Non-residents prevailed among the owners of CZK bonds (42.3%), their proportion mildly grew since the beginning of year 2018. Trend of cutting the net outlays on the state debt servicing continued. These costs were 16.9 CZK bn for H1 and decreased by nearly one sixth year-on-year, by nearly one half in the last six years.

Indebtedness rate of the government institution sector shrank year-on-year. Budget was in practice balanced, local government institutions attained surplus.

Consolidated debt of the whole government institutions sector[67] totalled 1 837 CZK bn according to the CZSO data at the end of Q1 2019 and was raised quarter-on-quarter (+102 CZK bn). Indebtedness rate was 34.0% of GDP, it fell by 1.8 p.p. year-on-year, solely thanks to the brisk growth of the nominal GDP. Government institution sector attained a very mild budget deficit in the amount of 2.3 CZK bn[68] in the CR in Q1, it showed nearly balanced budget also in the same period of the last year. Balance of central government institutions budget worsened by 9.6 CZK bn year-on-year and finished

[67] Preliminary data regarding the debt and deficit of the government institution sector for Q2 2019 will be published by CZSO on 2nd October 2019, by Eurostat then on 22nd October 2019.
[68] Balance of budget of government institutions adjusted for seasonal and calendar effects finished in surplus of 15.7 CZK bn for Q1, which constituted 1.1% of GDP. The adjusted surplus increased by 4.2 CZK bn against Q4 of the last year.

in 26.1 bn deficit, while the local government institutions budgeted with a surplus of 20.4 CZK bn (higher by 6.0 bn year-on-year). Budget of the social security funds (health insurance companies) did not change year-on-year and reached a surplus of 3.4 CZK bn.

The CR still maintained the position of fourth relatively least indebted EU economy.

The Czech Republic ranked the fourth relatively least indebted EU state at the end of Q1 2019. Only small economies of Estonia (8.1%) and Luxembourg (21.3%) recorded markedly favourable figures. Further five countries reached a similar indebtedness level as the CR. Indebtedness of the whole Union was 80.7% of GDP and did not reduce quarter-on-quarter for the first time since the beginning of year 2017. Small positive shift at the level of the whole Union is the result of prevailing high indebtedness of the majority of significant EU economies (apart from Germany). Indebtedness slightly enlarged in five EU countries year-on-year, beside others in Italy (to 134.0%), France (99.7%) and Greece (181.9%). Only less than half of the euro area members complied with the Maastricht deficit criterion at the level of 60% of GDP at the beginning of the year, only the Netherlands among the larger economies. Enduring economic growth was favourably reflected in the balance of the government institutions sector budget in the Union. It totalled (after adjustment for seasonal and calendar effects) only a shallow deficit (–0.6% of GDP) in Q1 and moved at the level of the business cycle peak from years 2007 and 2008 already second year in a row. Twelve union members reported surplus this year, five recorded deficit in the excess of 3% of GDP – Italy, France, Belgium and Romania like in the Q1 2018, Greece also joined this year.

Lowering of the indebtedness rate manifests only very slowly in EU, despite persisting economic growth as well as considerable reduction of budget deficit.